



KUMMISSJONI TAL-KOMUNITAJIET EWROPEJ

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RAKKOMANDEZZJONI TAL-KUMMISSJONI

**dwar l-aġġornament ta' l-2004 dwar il-Linji ta' Gwida Ġenerali tal-Politka Ekonomika
ta' l-Istati Membri u tal-Komunità (ghall-perjodu 2003-2005)**

(ippreżentat skond l-Artikolu 99(2) tat-Trattat KE)

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I. LINJI TA' GWIDA ĠENERALI DWAR IL-POLITIKA EKONOMIKA

1. L-ISTRATEĠIJA PREŻENTI TIBQA' VALIDA

Il-Kunsill adotta rakommandazzjoni fis-26 ta' Ġunju 2003 dwar il-Linji ta' Gwida Ġenerali dwar il-Politika Ekonomika ta' l-Istati Membri u tal-Komunità għall-perjodu bejn l-2003-2005¹. Dawn il-Linji ta' Gwida Ġenerali dwar il-politika ekonomika (BEPGs) jikostitwixxu l-istrateġija tal-politika ekonomika fuq iż-żmien mezzan ta l-UE. Il-BEPGs jiffokaw fuq il-kontribuzzjoni li l-politika ekonomika tista' tagħmel biex twettaq l-iskop strateġiku ta' Lisbona. Huma kkonċentri madwar:

- politika makroekonomika msejsafuq it-tkabbir u l-istabbiltà;
- riformi ekonomiċi sabiex joghla l-potenzjal tat-tkabbir ekonomiku ta' l-Ewropa; u
- it-tishih tas-sostenibilità.

Fl-isfond tar-riżultati ta' l-ewwel valutazzjoni tar-rapport mogħti lill-BEPGs ta' l-2003-05 kif ipprezentat fir-Rapport ta' Implimentazzjoni² u l-pariri mill-Kunsill Ewropew tar-Rebbiegha ta' l-2004, din ir-rakommandazzjoni tagħgħona u tikkompleta l-istrateġija preżenti. L-ebda emendi kbar tal-politika m'huma meqjusa neċessarji tant li jkun hemm bżonn bidla fil-linji ta' gwida ġenerali. L-enfażi f'dan l-aġġornament hu dwar l-integrazzjoni ta' l-għaxar Stati Membri godda fil-qafas ta' koordinazzjoni tal-politika ekonomika preżenti.

L-ewwel Parti ta' dan l-aġġornament tikkonċentra fuq il-konsiderazzjonijiet rilevanti sabiex jigu applikati l-linji ta' gwida fil-BEPGs ta' l-2003.05 lill-Istati Membri. Il-linji ta' gwida ġenerali preżenti jibqgħu validi u ma jinbidlux. Għandhom japplikaw fl-Istati Membri u fil-Komunità. Bl-iskop li tigi kkompletata l-istrateġija preżenti, il-Parti II tipprezenta rakommandazzjonijiet speċifiċi għall-pajjiżi ta' l-għaxar Stati Membri godda. Tinkludi wkoll aġġornamenti tan-noti tal-pajjiż għall-Ġermanja, il-Greċja, Franza, l-Italja, l-Olanda, il-Portugall u r-Renju Unit biex tippermetti emendi tal-politika fis-settur tal-politika tal-baġit.

2. SFOND EKONOMIKU MTEJJEB

L-irkupru ta' l-ekonomija fl-aħħar qed isehh fl-UE, appoġġjat mit-titjib ġenerali fl-ambjent internazzjonali. It-tkabbir tal-GDP beda jissahhah bil-mod il-mod mill-adozzjoni tal-BEPGs fis-sajf ta' l-2003, bl-esportazzjonijiet bhala l-mutur ewlieni għall-bidu ta' dan l-irkupru, minkejja t-tishih ta' l-ewro. Il-kundizzjonijiet huma wkoll mistennija jittjiebu fit-talba domestiku: il-fiduċja fost il-kumpaniji u l-konsumaturi qabdet, ir-rati ta' l-imghax qatt ma kienu daqsekk baxxi, u l-prezzijiet ta' l-ishma qegħdin jerġgħu jirkupraw. Fuq dan l-isfond, it-Thabbir Ekonomiku tar-Rebbiegha 2004 ibassar irkupru ieħor u t-tkabbir ekonomiku huwa mistenni li jilhaq il-potenzjal lejn l-aħħar ta' l-2004. Hemm bżonn li jissahhu dawn l-ewwel sinjali tat-tkabbir ekonomiku. Il-Kunsill Ewropew approva ufficialment f'Diċembru 2004 l-inizjattivi għat-tnedija ta' azzjoni mmirata bil-għan li jigi ffaċilitat tkabbir ekonomiku sostenibbli.

¹ Rakommandazzjoni tal-Kunsill tas-26 ta' Ġunju 2003 dwar il-Linji Ta' Gwida Ġenerali dwar il-politika ekonomika ta' l-istati Membri u tal-Komunità (għall-perjodu 2003.05), 2003/555/KE, ippubblikata fil-Gurnal Uffiċjali Nru L 195/1 ta' l-ewwel ta' Awissu 2003.

² Komunikkazzjoni tal-Kummissjoni 'L-ewwel Rapport ta' l-Implimentazzjoni tal-Linji ta' Gwida Ġenerali tal-Politika Ekonomika' KUMM(2004)20 finali, adottata fil-21 ta' Jannar 2004.

L-inflazzjoni hi mistennija li taqa' taht it-2 fil-mija waqt l-2004 u li terga' tonqos fl-2005. Filwaqt li zjiediet fil-prezzijiet amministrati u t-taxxi indiretti sejr in kollom effett li jghollu l-prezzijiet fl-2004, it-tnehhija ta' l-effett temporanju mill-ahhar zjiediet fil-prezzijiet ta' l-ikel ghandhom l-effett oppost. Bl-istess mod, iz-zjieda fil-valur ta' l-ewro sejra zzomm iz-zjieda fil-prezzijiet. Per eżempju, din assorbit bil-kbir iz-zjieda fil-prezz f'dollari taz-zejt. Minbarra dan, il-moderazzjoni tal-pagi hi mistennija tkompli fiz-zmien mezzan u bl-irkupru cikliku tal-produttività tax-xoghol, it-tkabbir fl-unità nominali ta' l-ispejjez tax-xoghol jistghu jaqghu konsiderevolment u b'hekk jikkontribwixxu għall-istabbiltà tal-prezzijiet.

Is-sitwazzjoni tas-suq tax-xoghol ghandha t-tendenza li tirrifletti l-izvilupp ekonomiku b'lura. Wara waqfa fl-2003, l-impjeg hu mistenni jibbenefika mill-attività ekonomika totali li regghet qabdet fit-tieni nofs tas-sena l-oħra. Madankollu, minhabba li l-irkupru jsehh gradwalment, l-impjeg huma mistennija jogħlew modestament din is-sena u jizdiedu b'qawwa ikbar is-sena d-dieħla.

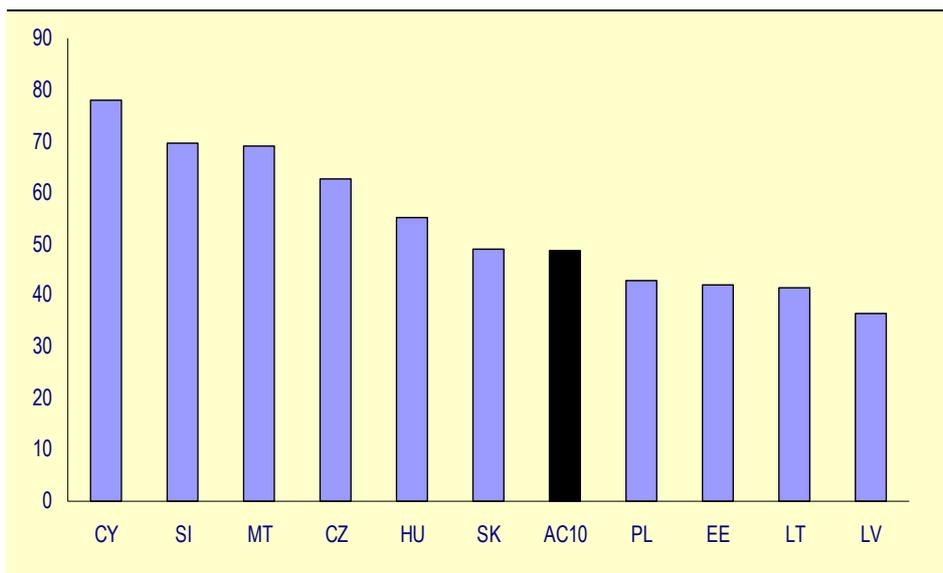
B'mod ġenerali, l-izviluppi ekonomiċi jwettqu l-istennija prevalenti meta tiġi adottata l-istrategija tal-politika ekonomika fuq iz-zmien mezzan; l-ekonomija qieghda tirkupra għalkemm b'pass moderat, u l-prospetti għall-2004.05 ma jippuntaw lejn l-ebda zbilanċ makroekonomiku li jehtieg bidla fil-politika. Fl-istess hin, it-tbassir juri li l-hila ta' l-aġġustament ta' l-ekonomija ta' l-UE u t-tkabbir potenzjali għadhom kajmani. Huwa għalhekk essenzjali li t-titjib tal-kundizzjonijiet ekonomiċi għandhom jiġu sfruttati kompletament sabiex jkun hemm progress deċisiv fl-geħluq tad- "differenza tal-kunsinna" f'termini ta' diskrepanza bejn il-mizuri tar-riforma strutturali kkunsidrati u dawk eventwalment adottati. Il-funzjonament mill-ġdid ta' l-attività ekonomika bħalissa jista' jissahħah aktar permezz ta' politika makroekonomika soda u permezz ta' implimentazzjoni ddeterminata tar-riformi ekonomiċi għat-tishih tat-tkabbir ekonomiku msemmija fil-BEPGs ta' l-2003-05.

3. L-INTEGRAZZJONI TA' L-GHAXAR STATI MEMBRI ĠODDA FIL-BEPGS TA' L-2003-05

L-adeżjoni ta' Ċipru, ir-Repubblika Ċeka, l-Estonja, l-Ungerija, il-Latvja, il-Litwanja, Malta, il-Polonja, is-Slovakkja u s-Slovenja fl-1 ta' Mejju 2004 sejra tkun grajja importanti hafna fl-istorja ta' l-Unjoni.

It-tkabbir se jikkontribwixxi għal dinamizmu ekonomiku ġdid b'effetti ta' tishih reċiproku. Il-potenzjal tat-tkabbir ekonomiku ta' l-Istati Membri l-ġodda hu stmat għal madwar 4 fil-mija kull sena, li jirrefletti *inter alia* il-progress sod tagħhom f'dawn l-ahhar snin b'rifomi strutturali u istituzzjonali. Is-Suq Intern ghanhu jitkabbar għal 455 miljun ċittadin. Minkejja l-progress reċenti, hemm bżonn li jingharaf li l-punt tat-tluq tagħhom kien differenti u li l-pajjiżi ta' l-adeżjoni sejr in għall-bidu jghoddu biss għal 5 fil-mija tal-GDP ta' l-Unjoni. B'livelli ta' dhul ta' inqas min-nofs ta' l-UE-15 medja (ara t-Tabella 1), l-isfidi ewlenien għall-pajjiżi ta' l-adeżjoni huma li jiżguraw konverġenza vera fuq medda twila ta' zmien, filwaqt li fl-istess hin jiksbu konverġenza nominali fit-terminu qasir sa medju.

Graff 1: GDP per capita 2003 (UE-15=100)



Sors: Servizzi tal-Kummissjoni (Eurostat, Indikaturi strutturali).

L-isfidi strutturali li jhabbtu wiċċhom magħhom l-Istati Membri ġodda mhumiex fundamentalment differenti minn dawk ta' l-istat attwali, anke jekk ċerti sfidi jitolbu iktar attenzjoni³. L-istrategija tal-politika ekonomika preżenti għalhekk tidher bħala xierqa b'mod ġenerali. L-iskala ta' l-isfidi ffaċċjati minn dawn il-pajjiżi tagħmilha kruċjali li jiffittex bilanċ xieraq bejn il-htigijiet politiċi differenti. Per eżempju, b'kunsiderazzjoni tal-bidla strutturali li għadha ma tlestietx lejn ekonomija tas-suq modewrn ibbażata fuq is-servizzi servizz modern ibbażat fuq suq ta' l-ekonomija, hafna mill-pajjiżi ta' l-adeżjoni għandhom bżonn politika li tiffavorixxi konvergenza vera. L-UE sejra tikkontribwixxi b'mod siewi għall-konvergenza vera billi tinvesti fir-regjuni li baqghu lura bis-sahha tal-fondi strutturali u ta' koeżjoni kif ukoll tal-Bank Ewropew ta' l-Investimenti. Madankollu, il-baġits nazzjonali għandhom ikopru r-rekwiżiti finanzjarji importanti maqghuda mal-bżonn biex tittejjeb il-bażi kapitali fiżika u umana, u l-awtoritajiet fiskali għandhom bżonn ilaħhqu mal-pressjonijiet tan-nefqa li ġejjin mit-tlestija tar-riformi ta' transizzjoni, waqt li jassiguraw onestà fiskali. Fl-istess waqt u b'kunsiderazzjoni għall-izbilanċ fl-estimi medji inizjali ta' xi 6 fil-mija tal-GDP, hemm bżonn li tiġi ggarantita l-konsolidazzjoni neċessarja għall-finanzi pubbliċi biex tissaħħaħ l-istabbiltà makroekonomika.

It-taqsimiet sussegwenti jirrevedu l-istrategija tal-politika ekonomika eżistenti u jagħtu importanza lil dawk il-linji ta' gwida ġenerali jew setturi tal-politika, fejn iċ-ċirkustanza speċifika ta' bosta mill-pajjiżi ta' l-adeżjoni huma tali li perjodu itwal ta' aġġustament ikun meħtieġ. Hemm bżonn li jiġi enfasizzat li d-differenzi huma differenti skond il-pajjiżi ta' l-adeżjoni. B'kunsiderazzjoni tad-differenzi fir-rendiment, il-prospetti, l-istrutturi u l-istituzzjonijiet ekonomiċi tagħhom, il-Parti II ta' dan l-aġġornament tipprezenta r-rakkomandazzjonijiet speċifiċi għall-pajjiż lill kull pajjiż ta' l-adeżjoni.

3.1 It-tkabbir ekonomiku u l-politika makroekonomika orjentata lejn l-istabbiltà

Politika makroekonomika soda għandha rwol kruċjali sabiex tappoġja t-tkabbir u l-impjieġ u sabiex iżzomm sod l-istabbiltà tal-prezzijiet. L-Istati Membri ġodda għandhom, bħal dawk attwali, jimmiraw biex jiksbu tkabbir ekonomiku ibbilanċjat sew li jwettaq kompletament il-potenzjal ta' dan it-tkabbir.

³ L-Ekonomija ta' l-Ewropa, karta okkażjonali Nru 4 "Sfidi strutturali ewlenija fil-pajjiżi ta' l-adeżjoni: l-intergrazzjoni tal-pajjiżi ta' l-adeżjoni fil-proċessi ta' koordinazzjoni tal-politika ta' l-ekonomija tal-Komunità" minghand il-Kumitat tal-Politika ta' l-Ekonomija, Lulju 2003.

Minbarra dan, għal dak li għandu x'jaqsam ma' bosta mill-pajjiżi ta' l-adeżjoni, il-politika makroekonomika għandha tappoġġja wkoll il-bidla strutturali li fadal lejn ekonomika b'iktar servizzi.

L-Istati Membri godda għandhom bżonn ifittxu sinergija b'saħħha bejn ir-riformi strutturali neċessarji u l-politika makroekonomika li ssahħah l-istabbiltà. L-iskemi tar-rata tal-kambju jikkostitwixxu parti importanti tal-qafas tal-politika ekonomika u monetarja kumplessiva u għandhom jiġu orjentati sabiex jiksbu konverġenza nominali reali u sostenibbli. Il-parteciġazzjoni fl-ERM II, f'xi fażi wara l-adeżjoni, għandha tgħin dawk it-tentattivi. Politika monetarja kredibbli għandha tippermetti iżjed tnaqqis fir-rati ta' l-imghax fit-tul li jwassal għal kemm għall-investiment għoli tant meħtieġ kif ukoll għall-konsolidazzjoni fiskali.

Għal dak li għandu x'jaqsam mal-bżonn li "jintlaħqu u jinżammu pożizzjonijiet baġitarji sodi", għandha tinstab medda ta' żmien xierqa bejn il-heffa tal-konsolidazzjoni tal-baġit neċessarja u l-pożizzjoni fiskali xierqa li tappoġġja t-transizzjoni. Is-sorveljanza tal-baġit għal dak li jikkonċerna l-Istati Membri godda għandha tibda bl-eżami tal-Programmi ta' Konverġenza tagħhom. Għandha tinghata attenzjoni partikolari liċ-ċirkostanzi speċifiċi tal-pajjiż, b'mod partikolari lill-pożizzjonijiet tal-baġit tal-bidu, il-bidliet strutturali li għaddejjin fl-ekonomiji u r-riskji possibbli li jirriżultaw mill-iżbilanċi fil-kontijiet kurrenti u t-tkabbir qawwi tal-kreditu. Jista' jkun xieraq, minn punt ekonomiku, li jithalla perjodu għall-aġġustament annwali f'ċerti każijiet fejn hemm bżonn li jiġi korrett deficiet ta' iktar minn 3 fil-mija. Dan jippermetti lill-Istati Membri biex jikkonsolidaw il-finanzi pubbliċi tagħhom b'mod sostenibbli, filwaqt li fl-istess ħin itemmu r-ristrutturar ta' l-ekonomija. B'mod ġenerali, l-effiċjenza ta' l-infiq pubbliku tista' tittejjeb konsiderevolement, inter alia bis-saħħa ta' ridirezzjoni ta' l-infiq pubbliku lejn investimenti li jġibu t-tkabbir u li jipproduċu riżultati effettivi għal infiq li mhux eċċessiv: investimenti fil-kapital fiżiku u uman u fir-riċerka u l-innovazzjoni. Barra minn dan, twessigh tal-bażi tat-taxxi fuq ix-xogħol u titjib tal-ġbir tat-taxxi sabiex jiġi żgurat id-dhul meħtieġ jista' jiffaċilita tnaqqis fir-rati ta' taxxa fuq ix-xogħol (inklużi rati għolja ta' kontribuzzjonijiet tas-sigurtà soċjali).

Tabella 1: Indikaturi Makroekonomiċi għall-Istati Membri godda u daww preżenti fl-2003

	AC10	UE15
Tkabbir GDP (reali, % p.a.)	3.6	0.8
Inflazzjoni (% p.a.)	2.1	2.0
Kont kurrenti(% tal-GDP)	-3.7	0.2
Qgħad (%)	14.3	8.0
Bilanċ tal-Gvern (% tal-GDP)	-5.7	-2.6
AC10= l-ghaxar pajjiżi ta' adeżjoni.		
Sors: Servizzi tal-Kummissjoni (inkluż Eurostat, Indikaturi strutturali).		

Id-deficiet attwali kien jgħodd għal medja xi 4.5 fil-mija tal-GDP fl-2003 fl-Istati Membri godda, u dan jirrifletti l-proċess li qed jgħaddu minnu dawn il-pajjiżi biex ilaħħqu ma' l-oħrajn u l-lakuni kbar fiit-tfaddil-investiment domestiku. Sfida kbira tal-politika makroekonomika għal xi uħud minn dawn il-pajjiżi ta' l-adeżjoni tikkonsisti għalhekk f'li jzommu deficiets relattivament għolja fil-limiti li fihom jista' jiġi żgurat finazjament estern sod. F'dan ir-rigward, it-trażzin fiskali u l-htieġa li tiġi evitata politika pro-ċiklika se jkun essenzjali sabiex jitnaqqsu d-deficiets attwali, minhabba li l-finazjament tagħhom jista' jsir aktar diffiċli wara li jitlesta għal kollox il-proċess ta' privatizzazzjoni.

Ambjent makroekonomiku stabbli jeħtieġ żjidi nominali fil-pagi li huma konsistenti kemm ma' l-istabbiltà tal-prezzijiet kif ukoll mal-kisbiet fil-produttività. Se jkun importanti wkoll għall-holqien tal-pagi fil-pajjiżi ta' l-adeżjoni li jkun appoġġ għar-ristrutturar ta' l-ekonomija li jsir mezz biex il-pagi jirriflettu aħjar id-differenzi fil-kundizzjonijiet tas-suq tax-xogħol lokali li hemm bejn ditti, setturi,

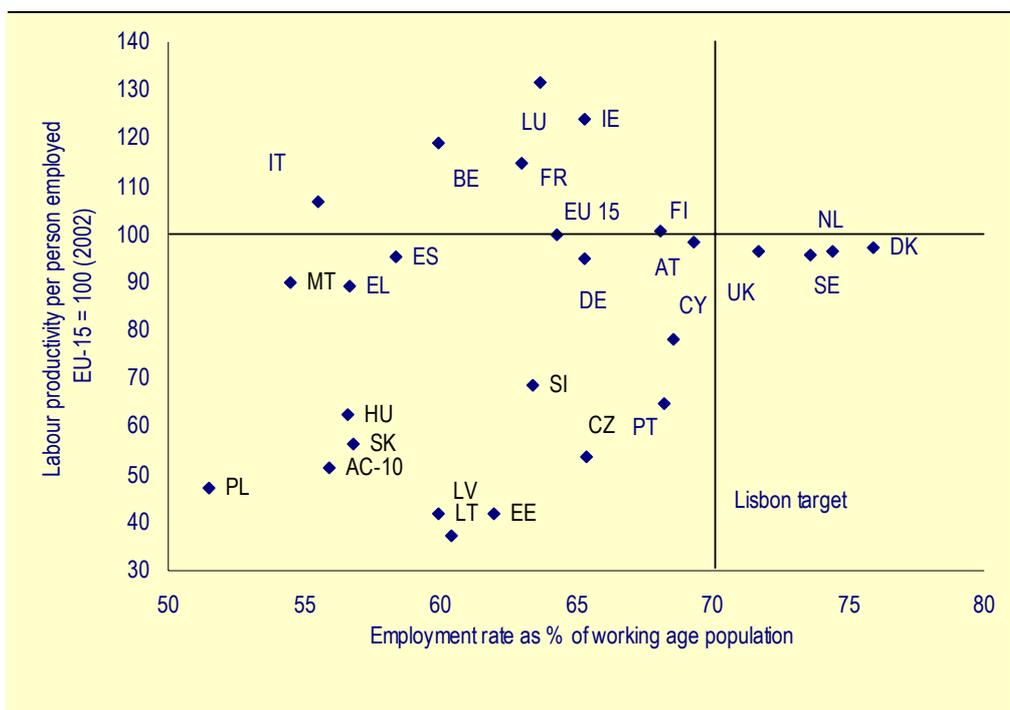
reġunijiet u xogħlijiet differenti. Lil hinn min dan, żviluppi reali fil-pagi jridu jappoġġjaw il-kompettività esterna fl-Istati Membri fid-dawl ta' l-htieġa li jiġi attirat l-investment barrani dirett.

3.2 Riformi ekonomiċi sabiex jiżied il-potenzjal ta' l-Ewropa għat-tkabbir ekonomiku

Il-proċess ta' tlaħħiq ma' l-oħrajn fil-livelli tad-dhul huwa proċess fuq medda twila ta' żmien. Se jkun kruċjali li tidjieg il-qasma bejn ir-rati ta' l-impjieg u l-livelli ta' produttività bejn il-pajjiżi ta' l-adeżjoni u l-UE-14. Il-linji ta' gwida eżistenti li jimmiraw għal 'xogħol aktar u aħjar' u 'ż-żjieda fil-produttività u d-dinamiżmu tan-negozju' huma implimentati l-aħjar b'mod komprensiv u koordinat.

Il-kontibuzzjoni li l-politika ta' l-impjieg tista' tagħti hija riflessa fil-linji ta' gwida eżistenti li jagħfsu fuq il-kunċett ta' li 'nġieghlu x-xogħol iħallas' u fuq li nipprezzaw in-nies lura fix-xogħol, l-aktar dawk ta' hiliet u snajja' limitati jew dawk li jgħixu f'reġjuni ifqar. Il-qagħda tas-suq tax-xogħol hija konsiderevolment aghar fil-pajjiżi ta' l-adeżjoni, b' rati ta' l-impjieg huma jew weqfin jew inkella neżlin, rati ta' qgħad għoljin (li wkoll għandhom tendenza jkunu fuq medda twila ta' żmien u jolqtu l-aktar liż-żgħażaġh), numri kbar ta' persuni mhux attivi u setturi informali mdaqqsin. Se jkun għalhekk essenzjali li l-isforzi politiċi jagħfsu fuq numru żgħir ta' oqsma prioritarji li aktarx jista' jkollhom l-akbar impatt fuq ir-rendiment tas-suq tax-xogħol: li jkun żgurat li l-iżviluppi reali fil-pagi jirriflettu t-tkabbir fil-produttività; it-titjib ta' l-inċentivi finanzjarji għax-xogħol bis-sahha ta' riforma fuq is-sistemi tat-taxxa / tal-benefiċċji soċjali; it-titjib tal-formazzjoni tal-kapital uman; u t-tehid ta' riformi xierqa fir-regolamenti tas-suq tax-xogħol. Il-politika dwar l-impjieg trid tappoġġja l-proċess li għaddej taċ-ċaqliq strutturali kbir fil-kompożizzjoni settorjali u reġjonali ta' l-impjieg.

Graff 2: Impjieg u livelli ta' produttività fl-Istati Membri ta' l-UE u pajjiżi ta' adeżjoni (2002)



Sors: Servizzi tal-Kummissjoni Eurostat, Indikaturi strutturali).

Se jkun essenzjali li jiżiedu r-rati ta' l-impjieg u li fl-istess hin jittejjeb it-tkabbir tal-produttività għall-Istati Membri (ara Graff nru 2). Ir-ristrutturar li għaddej fl-ekonomija ta' dawn il-pajjiżi huwa strumentali fit-titjib tal-livell ta' produttività li generalment huwa baxx. It-transizzjoni minn speċjalizzazzjoni f'attivitajiet ta' valur miżjud baxx jew valur tax-xogħol baxx lejn attivitajiet ta' valur miżjud għoli għandu jkoll il-vantaġġi komparattivi attwali. L-integrazzjoni ekonomika akbar fis-Suq

Intern u l-miżuri li jakkumpanjawha sabiex jippromwovu l-kompetizzjoni fl-ekonomija għandhom jgħaġġlu l-proċess tar-ristruttar fl-Istati Membri ġodda. Il-kompetizzjoni akbar tehtieg proċess aktar mgħaġġel fil-privatizzazzjoni, tnaqqis fil-piż regolatorju fuq in-negozju u appoġġ akbar għall-intraprenditorjat. F'dan il-kuntest, trid tissahha il-hila ta' l-awtoritajiet ċentrali u lokali biex jinfurzaw il-htigijiet leġislattivi, l-aktar f'dak li għandu x' jaqsam mar-regoli legali dwar id-dhul fis-suq u l-hruġ minnu tal-kumpaniji.

Tabella 2: Indikaturi Ekonomiċi għall-Istati Membri ġodda u daww prezenti fl-2003

	AC10	UE15
GDP per capita ¹	48.7	100
Produttività għal kull persuna impjegata ²	53.6	100
Rata ta' Impjegi (fl-2002) ³	55.9	64.3
Investimenti tan-Negozju (% tal-GDP) ⁴	17.9	17.2
Total ta' FDI inflows (% tal-GDP) ⁵	5.0	4.4
Nefqa R&D (% tal-GDP) ⁶	0.83	1.98

¹ f' PPS, livell, UE15=100. ² GDP f' PPS għal kull persuna impjegata, livell, UE15=100.

³ Rata ta' impjegi totali – Persuni impjegati li għandhom età ta' 15-64 bhala porzjoni tal-popolazzjoni totali ta' l-istess faxxa ta' età, 2002. ⁴ Investimenti ta' kapital gross fiss mis-settur privat, 2001 għal AC10 u 2002 għal UE15. ⁵ 2002. ⁶ Nefqa gross domestika fuq R&D, 2001.

Sors: Servizzi tal-Kommissjoni (inkluz Eurostat, indikaturi strutturali).

It-tkabbir fil-produttività se jitjeb aktar bit-transizzjoni ta' l-Istati Membri ġodda għal ekonomija msejsa fuq l-għerf, li hija fil-qofol ta' l-istrategija UE ta' Lisbona. Barra minn dan, l-Inizjattiva Ewropea għat-Tkabbir Ekonomiku tishaq dwar l-importanza ta' l-investimenti f' netwerks u fir-riċerka bhala passi kruċjali lejn l-ghoti ta' spinta lit-tkabbir ekonomiku, integrazzjoni aħjar ta' Ewropa mkabbra, u t-titjib ta' produttività u l-kompetittività. Għall-Istati Membri ġodda, it-tixrid u t-tasferimenti teknoloġiċi R&D huwa importanti kemm bhala investiment R&D kif ukoll bhala għodda biex jgħaġġlu t-transizzjoni lejn attivitajiet ta' valur miżjud oghla. Huwa essenzjali li jiġi sostnut livell għoli ta' investiment dirett barrani f'dan l-isforz kollu, bhal ma huwa daqstant importanti li jkun hemm tweġiba aħjar u akbar għas-sistema ta' edukazzjoni u taħriġ għall-htigijiet li dejjem qed jinbidlu tas-suq tax-xogħol. Ir-riformi tas-sistemi ta' edukazzjoni u taħriġ jistgħu wkoll jgħinu sabiex jheggu għal mixja lejn attivitajiet li huma aktar innovattivi u msejsa b'mod instensiv fuq l-għerf, kif ukoll l-investimenti fit-teknoloġija ambjentali.

Rwol importanti fl-allokkazzjoni u d-direzzjoni ta' flejjes lejn investimenti produttivi u lejn fiduċja akbar ta' l-investitur jinvolve is-swieq kapitali żviluppata li jahdmu minghajr xkiel żejjed. Filwaqt li, fil-pajjiżi ta' l-adeżjoni, is-swieq kapitali ilhom jikbru mill-bidu tad-Disgħinjiet (kemm f'dak li għandu x'jaqsam ma' daqs u valur), jibqgħu ġeneralment sottosviluppata fil-konfront ta' bosta Stati Membri attwali (minbarra Ċipru u Malta). L-integrazzjoni rapida fis-suq uniku għas-servizzi finanzjarji bis-saħħa ta' traspozizzjoni u implimentazzjoni f'waqtha ta' l-*acquis* kollu f'dan il-qasam, se jkun dejjem aktar importanti għall-appoġġ ta' l-iżvilupp ta' settur finanzjarju sod u kkapitalizzat sew u għaž-żamma ta' ambjent ugħali għal kulhadd f'dak li għandu x'jaqsam ma' l-istituzzjonijiet finanzjarji f' Unjoni Ewropea mkabbra. Barra minn hekk, is-swieq kapitali f'bosta Stati Membri ġodda huma kkaratterizzati minn livell għoli ta' intermedjazzjoni bankarja (tipikament aktar minn 80 fil-mija ta' l-assi finanzjarji totali fl-Ewropa Ċentrali u l-Istati Baltiċi) u fenomenu estensiv ta' sidien barranin ta' banek tal-pajjiż (minbarra f' Ċipru u s-Slovenja), filwaqt li bosta qed jaraw żvilupp mgħaġġel ta' intermedjarji finanzjarji oħra bhal fondi tal-pensjonijiet (eż. Il-Polonja). F'dan il-kuntest, se jkun partikolarment importanti għall-Istati Membri ġodda li jkomplu jsaħħu l-arranġamenti ta' supervizjoni finanzjarja

tagħhom u jtejbju l-kooperazzjoni minn fruntiera għall-oħra fis-superviżjoni finanzjarja u fil-*crisis management* finanzjarju.

3.3 It-tishih tas-sostenibbiltà

Il-BEPGs jagħmlu enfazi konsiderevoli fuq li jiġi żgurat li t-tkabbir ekonomiku huwa sostenibbli fl-UE, billi jiġu integrati s-sostenibbiltà ekonomika, soċjali u ambjentali fl-istrategija tal-politika ekonomika.

Popolazzjoni li qed tixjeh sejra timplika sfidi simili għas-sostenibbiltà ekonomika fl-Istati Membri u fl-UE 15. Filwaqt li ġeneralment il-punt tat-tluq tagħhom huwa aħjar (b'liveli ta' dejn inqas f'bosta każi), il-ġejjieni demografiku x'aktarx ikollu implikazzjonijiet ekonomiċi u soċjali) akbar.

Tabella 3: Indikaturi ta' sostenibilità għall-Istati Membri ġodda u dawk preżenti

	AC10	UE15
Dejn tal-Gvern (2003, % tal-GDP)	42.2	64.0
Rata ta' impjiegi ta' haddiema anzjani ¹	30.4	40.1
Rata ta' impjiegi fit-tul ¹	8.1	3.0
Emissjonijiet ta' Greenhouse gas ²	69	98
Intensità ta' enerġija ³	709	194

¹ Figuri għal 2002. ²Figuri għal 2001, 1990 sena bażi =100. ³ konsum ta' l-enerġija fl-2001 diviż mill-GDP b' prezzijiet kostanti, kilogramma ta' żejt ekwivalenti għal kull 1000 Ewro.

Sors: Servizzi tal-Kummissjoni (inkluż. Eurostat, indikaturi strutturali).

Fil-qofol, il-politika ekonomika soda tagħti kontribut importanti lis-sostenibbiltà soċjali minhabba li x-xogħol għandu sehem vitali f'li johroġ in-nies mill-faqar u mill-eskluzjoni soċjali. Fl-Istati Membri ġodda, trid issir enfazi addizzjonali fuq l-immodernizzar tas-sistemi ta' protezzjoni soċjali u t-titjib tal-hiliet tal-haddiema, bil-għan li jiżdienu r-rati ta' parteċipazzjoni u tittejjeb il-mobilità. Ir-rati baxxi ta' qgħad, kemm tal-haddiema żgħażaġħ kif ukoll ta' dawk ikbar, tehtieg atenzjoni speċjali f'dan ir-rigward. Għandhom jiġu indirizzati d-differenzi reġjonali l-kbar, l-aktar billi jiġi żgurat li jkun hemm investimenti effiċjenti u differenzjazzjoni xierqa tal-pagi (li tirrifletti d-differenzi fil-produttività). Barra minn hekk, l-ambjent tan-negozju għandu jittejjeb, speċjalment bis-saħħa ta' miżuri għall-bini ta' hiliet fit-tmexxija pubblika. Dan għandu wkoll ittejjeb l-effiċjenza fl-użu tal-fondi Strutturali u ta' Koeżjoni ta' l-UE.

L-investimenti sostanzjali fl-infrastruttura ta' l-enerġija u t-trasport li huma tant mehtieġa fil-biċċa l-kbira ta' l-Istati Membri ġodda għandhom il-għan li jnaqqsu l-impatti ambjentali ta' l-użu ta' l-enerġija u t-trasport u li jtejbju l-effiċjenza ta' l-enerġija. Investimenti bħal dawn se jkunu kruċjali minhabba li l-intensitajiet enerġetiċi tagħhom jaqbzju 'l dawk ta' l-Istati Membri attwali kważi b' 4 darbiet, ara Tabella Nru 3, minkejja tittejjeb ta' 6% fis-sena tul l-aħħar għaxar snin. Se jkun partikolarment essenzjali li jitqiesu sew l-ispejjeż involuti fil-konfront tad-dannu ambjentali meta jsiru deċiżjonijiet dwar l-investment, inkluż it-tnaqqis tas-sussidji għall-enerġija u l-introduzzjoni ta' taxxi u charges xierqa, għal per eżempju il-konsum ta' l-enerġija u/jew l-użu tat-trasport.

II. LINJI TA' GWIDA TA' POLITIKA EKONOMIKA SPECIFIKA GHALL-PAJJIŻ

Part II contains updates of the country-notes for Germany, Greece, France, Italy, the Netherlands, Portugal and the United Kingdom. It also presents country-notes for the ten new Member States.

The Council adopted the broad guidelines of the economic policies for the 2003-05 period for the current Member States on 26 June 2003. The country-specific recommendations therein generally remain valid, although some of them need to be updated to allow for necessary policy adjustments in the area of budgetary policies.

It is important to note that, even when measures have been taken that partly or even fully address a particular recommendation, that recommendation is not updated until a full assessment of their impact can be carried out. The pace and nature of progress in the implementation of the various guidelines is reviewed in the annual Implementation Report.

1. Il-Belġju

No update.

2. Id-Danimarka

No update.

3. Il-Ġermanja

One of the challenges facing Germany is to “reduce rapidly the general government deficit to below 3 per cent of GDP and keep government finances on a steady consolidation path”. In order to achieve this, Germany was recommended in the 2003 version of the Broad Economic Policy Guidelines to:

- ensure a rigorous budget execution and implement the announced or compensatory measures for 2003 amounting to 1 per cent of GDP and put an end to the present excessive deficit situation by 2004 at the latest (recommendation 6); and
- lower the cyclically-adjusted deficit by at least one percentage point of GDP between the end of 2003 and 2005 (recommendation 7).

These two recommendations were similar to those addressed by the Council to Germany on 21 January 2003 in accordance with Articles 104(7) of the Treaty. On 18 November 2003, the Commission adopted two recommendations on the basis of Article 104(8) and 104(9) respectively for the Council to decide (1) that action taken by Germany was inadequate to bring the excessive deficit to an end and (2) to give notice to Germany to take the necessary measures to bring the general government deficit below 3 per cent of GDP in 2005 at the latest. On 25 November 2003, the Council did not adopt the two Commission recommendations but adopted instead a set of conclusions endorsing, *inter alia*, the commitments made by Germany to reduce the cyclically-adjusted deficit by 0.6 per cent of GDP in 2004, and by 0.5 per cent of GDP or a larger amount in 2005 so as to ensure that the general government deficit would be brought below 3 per cent of GDP in 2005. In its Opinion on the 2003 update of the stability programme of Germany⁴, the Council reaffirmed these conclusions.

⁴ OJ C68, 18.3.2004.

In the light of these developments and bearing in mind that budgetary plans for the years beyond 2005 are to an important extent formed within the period covered by the BEPGs (*inter alia* in the multi-annual stability programmes), recommendations 6 and 7 are replaced by the following:

- “6. achieve an annual reduction in the cyclically-adjusted deficit of 0.6 per cent of GDP in 2004 and of at least 0.5 per cent of GDP or a larger amount in 2005 so as to ensure that the general government deficit is brought below 3 per cent of GDP in 2005 (GL 1);
7. should the recovery in economic activity be stronger than currently expected, allocate any higher-than-expected revenues to deficit reduction and accelerate the reduction in the cyclically-adjusted deficit;
- 7bis ensure that the budgetary consolidation continues in the years after 2005, namely through a steady reduction in the cyclically-adjusted budgetary deficit by at least 0.5 percentage points of GDP per year or more if necessary to achieve the medium term position of government finances close to balance or in surplus and bring back the debt ratio to a declining path (GL 1).”

4. II-Grečja

One of the challenges facing Greece is to “ensure the long-term sustainability of public finances in the face of population ageing, in particular in view of the high government debt ratio”. In order to achieve this, Greece was *inter alia* recommended in the 2003 version of the Broad Economic Policy Guidelines to:

- ensure effective control of government current primary spending by addressing resolutely the problem of the inelastic elements of expenditures, e.g. the wage bill (recommendation 2).

The fiscal data for 2003 show that the general government deficit stayed only just below the 3 per cent of GDP reference value. This represents a considerable widening of the deficit compared to 2002 in spite of a positive output gap, reflecting the pro-cyclical, expansionary nature of Greek fiscal policies. For 2004, there is a distinct risk that the reference value for the deficit may be breached. Greece is moving further away from a budgetary position of close to balance or in surplus..

In the light of these developments, recommendation 2 is replaced by the following:

- “2. until a medium-term position of close to balance or in surplus is achieved, ensure an improvement in the cyclically-adjusted budget balance of at least 0.5 per cent of GDP per year, specifically through effective control of government current primary spending, and stand ready to take further measures to avoid the occurrence of an excessive deficit (GL 1).”

5. Spanja

No update.

6. Franza

One of the challenges facing France is to “reduce rapidly the general government deficit to below 3 per cent of GDP and keep government finances on a steady consolidation path”. In order to achieve this, France was recommended in the 2003 version of the Broad Economic Policy Guidelines to:

- achieve a significantly larger improvement in the cyclically-adjusted deficit in 2003 than that currently planned (recommendation 1);

- implement measures ensuring that the cyclically-adjusted deficit is reduced in 2004 by 0.5 per cent of GDP, or by a larger amount, so as to ensure that the cumulative improvement in 2003-2004 is enough to bring the nominal deficit below 3 per cent in 2004 at the latest (recommendation 2); and
- limit the increase in the general government gross debt to GDP ratio in 2003 (recommendation 3).

These three recommendations were similar to those addressed by the Council to France on 3 June 2003 in accordance with Article 104(7) of the Treaty. On 8 and 21 October 2003 respectively, the Commission adopted two recommendations on the basis of Article 104(8) and 104(9) respectively for the Council to decide (1) that no effective action had been taken by France in response to the recommendation of 3 June and (2) to give notice to France to take the necessary measures to bring the government deficit below 3 per cent of GDP in 2005 at the latest. On 25 November 2003, the Council did not adopt the two Commission recommendations but adopted instead a set of conclusions endorsing, *inter alia*, the commitments made by France to reduce the cyclically-adjusted deficit by 0.8 per cent of GDP in 2004, and by 0.6 per cent of GDP or a larger amount in 2005 so as to ensure that the general government deficit would be brought below 3 per cent of GDP in 2005. In its Opinion on the 2003 update of the stability programme of France⁵, the Council reaffirmed and further clarified these conclusions.

In the light of these developments and bearing in mind that budgetary plans for the years beyond 2005 are to an important extent formed within the period covered by the BEPGs (*inter alia* in the multi-annual stability programmes), recommendations 1, 2 and 3 are replaced by the following:

- “1. achieve an annual reduction in the cyclically-adjusted deficit of 0.8 per cent of GDP in 2004 and of at least 0.6 per cent of GDP or a larger amount in 2005 so as to ensure that the general government deficit is brought below 3 per cent of GDP in 2005 (GL 1);
2. should the recovery in economic activity be stronger than currently expected, allocate any higher-than-expected revenues to deficit reduction and accelerate the reduction in the cyclically-adjusted deficit through the implementation of additional measures. In addition, any budgetary margin stemming from a slower than planned increase in expenditures should be allocated to deficit reduction;
3. ensure that the budgetary consolidation continues in the years after 2005, namely through a steady reduction in the cyclically-adjusted budgetary deficit by at least 0.5 percentage points of GDP per year or more if necessary to achieve the medium term position of government finances close to balance or in surplus and bring back the debt ratio to a declining path (GL 1).”

7. L-Irlanda

No update.

8. L-Italja

One of the challenges facing Italy is to “rapidly consolidate public finances”. In order to achieve this, Italy was *inter alia* recommended in the 2003 version of the Broad Economic Policy Guidelines to:

- Until a medium-term budget position of close to balance or in surplus is achieved, ensure a reduction in the cyclically-adjusted deficit of at least 0.5 per cent of GDP per year, replacing one-off measures by measures of a more permanent character (recommendation 1).

⁵ OJ C43, 19.2.2004.

The fiscal data for 2003 show that the general government deficit was 2.4 per cent of GDP, almost unchanged compared to 2002 (2.3 per cent). In a context of weak economic growth, the authorities have continued to rely on temporary measures to restrain the deficit. Such measures are estimated to have improved the budgetary outturn by slightly more than 2 percentage points of GDP (around 1.5 percentage points in 2002). Markedly lower interest expenditure compared to the previous year also helped stave off a larger increase in the deficit. In 2004, with reliance of one-off measures to be reduced by half, there is a distinct risk that the 3 per cent of GDP reference value for the deficit may be exceeded. With the output gap practically unchanged, the development in the cyclically-adjusted balance is also unfavourable. The adjustment towards a position close to balance in cyclically-adjusted terms is further set back.

In light of these developments, recommendation 1 is replaced by the following:

- “1. until a medium-term position of close to balance or in surplus is achieved, ensure an improvement in the cyclically-adjusted budget balance of at least 0.5 per cent of GDP per year, replacing one-off measures by measures of a more permanent character, and stand ready to take further measures to avoid the occurrence of an excessive deficit (GL 1).”

9. II-Lussemburgu

No update.

10. L-Olanda

One of the challenges facing the Netherlands is to “pursue budgetary adjustment in the coming years in the face of weaker potential growth, and the budgetary costs of ageing”. In order to achieve this, the Netherlands was recommended in the 2003 version of the Broad Economic Policy Guidelines to:

- continue to contain government expenditure within clearly defined ceilings set in real terms, consistent with a budgetary position close to balance or in surplus (recommendation 1).

The fiscal data for 2003 show that the general government deficit stayed only just below the 3 per cent of GDP reference value. This is linked to the sharp economic downturn, which led to a stronger-than-expected increase in the deficit, despite a substantial package of fiscal savings. For 2004, there is a risk that the 3 per cent of GDP reference value for the deficit might be exceeded. However, taking into account the widening of the output gap, the development of the cyclically-adjusted balance is more favourable. In cyclically-adjusted terms an adjustment towards a position close to balance is well underway.

In the light of these developments, recommendation 1 is replaced by the following:

- “1. continue to contain government expenditure within clearly defined ceilings set in real terms, consistent with a medium-term budgetary position close to balance or in surplus and stand ready to take further measures to avoid the occurrence of an excessive deficit (GL 1 and 14).”

11. L-Awstrija

No update.

12. II-Portugall

One of the challenges facing Portugal is to “accelerate the consolidation of public finances and address the strong dynamics of government expenditure”. In order to achieve this, Portugal was inter alia recommended in the 2003 version of the Broad Economic Policy Guidelines to:

- ensure that the government deficit is further reduced in 2003 as planned and that the cyclically-adjusted deficit is thereafter lowered by at least 0.5 per cent of GDP a year in order to reach a budget position that is close to balance (recommendation 1).

The fiscal data for 2003 show a general government deficit of 2.8 per cent of GDP, thereby in compliance with the Council Recommendation of 5 November 2002 addressed to Portugal under Article 104(7) of the Treaty, which called for a government deficit below the 3 per cent of GDP reference value by 2003 at the latest. The large negative output gap associated with the economic recession of 2003 hindered considerably the process of budgetary consolidation, because of the massive shortfall in tax revenue that developed during 2003 (excluding the one-off measure on the sale of tax and social contributions arrears). Although the government has been broadly successful in securing the planned restraint of expenditure (i.e. growth in current primary expenditure continued to decelerate from 8.9 per cent in 2001 to 7.8 per cent in 2002 and 4.1 per cent in 2003), the shortfall in tax revenue induced by the recession led the government to rely, to a significant degree, on one-off measures for a second consecutive year (1.5 and 2.1 per cent of GDP in 2002 and 2003 respectively). For 2004, there is a distinct risk that the reference value for the deficit may again be exceeded in view of slow growth and the only partial replacement planned so far of the significant amount of one-off measures adopted in 2003.

In light of these developments, recommendation 1 is replaced by the following:

- “1. until a medium-term position of close to balance or in surplus is achieved, ensure an improvement in the cyclically-adjusted budget balance of at least 0.5 per cent of GDP per year, replacing one-off measures by measures of a more permanent character, and stand ready to take further measures to avoid that the deficit breaches the 3 per cent of GDP reference value again (GL 1).”

13. Il-Finlandja

No update.

14. L-Isvezja

No update.

15. Ir-Renju Unit

The fiscal data for 2003 show that the general government deficit was 3.2 per cent of GDP, above the 3 per cent of GDP reference value. The budgetary position deteriorated more than planned in 2003 due principally to weaker-than-expected direct tax receipts. In the medium term, both the headline and cyclically-adjusted deficits are projected to decline to just below 2 per cent of GDP, in the context of continuing increases in planned expenditure aimed at addressing past under-investment by the public sector and under-provision of public services. The projected deficit path does not, however, allow a sufficient safety margin to prevent a breach of the 3 per cent of GDP reference value with normal macroeconomic fluctuations. Furthermore, there are risks to the budgetary projections stemming from the assumed autonomous rise in the revenue ratio.

In the light of these developments, the United Kingdom faces an additional challenge compared to the 2003 version of the Broad Economic Policy Guidelines, namely to:

Strengthen the budgetary position so as to avoid emerging budgetary imbalances

In order to strengthen the budgetary position so as to ensure sound public finances, the United Kingdom is recommended to:

- “6. improve the cyclically-adjusted position to consolidate the public finances, consistent with a budgetary position of close to balance or in surplus in the medium term, and stand ready to take further measures so as to endeavour to avoid the occurrence of an excessive deficit (GL 1).”

16. Ċipru

The small economy, with tourism as a mainstay, has shown some resilience in the face of a difficult international environment. At first, steady and high real GDP growth averaging 4.2 per cent for 1997-2001 was driven both by domestic demand and continued high growth in tourist arrivals. However, after 11 September 2001 the economy was hit by the slump in tourism linked to international terrorist threats, war in Afghanistan and Iraq, and SARS, with the decline continuing in 2003. Growth therefore more than halved but still reached 2 per cent in 2002 and 2003, supported by moderate domestic demand. This is however below potential growth.

The relatively good growth performance was supported by a market economy dominated by the private sector and with, *inter alia*, a highly developed financial and legal system, generally prudent economic policies, and a flexible labour market. The latter has been operating close to full employment and with high participation rates; with unemployment rates fluctuating between 3-5 per cent, Cyprus effectively does not have an unemployment problem. At the same time, the crisis in (mass-) tourism in Cyprus has underlined the increasing economic dependence on this sector, while traditional sources of export earnings, particularly within the manufacturing sector, show a structural decline. Therefore, Cyprus may have an interest in increasing its diversification towards higher value added activities. To this end, Cyprus may accelerate the transition toward a knowledge-based economy and continue to simplify the business environment.

A fiscal consolidation plan was introduced in 1999 and revised and extended in following years. However, fiscal performance in 2002 and 2003 slipped again and consolidation was effectively abandoned as deficits increased to 4.6 per cent and 6.3 per cent of GDP respectively. The expansionary fiscal stance contributed to an increase in domestic demand and a current account deficit projected at 4.4 per cent of GDP for 2003. The government intends to tackle anew the fiscal deficit for this and following years, thus working towards a more favourable policy mix and supporting a narrowing of the current account deficit.

Policies in Cyprus should aim at achieving a high degree of sustainable convergence, in particular as regards the consolidation of public finances. Both the further consolidation of public finances and management of the increasing tourism dependence need to be supported by policies which assist in perpetuating the strong growth performance into the medium and long term. This requires in particular a strengthening of the growth and employment base and Cyprus should continue its further transition to a knowledge-based economy. Against this background, Cyprus faces two major challenges:

- Ensure a reduction of the general government deficit on a sustainable basis,
- Increase the diversification of the economy towards higher value added activities.

Ensure a reduction of the general government deficit on a sustainable basis

Fiscal consolidation went increasingly off target in 2002 and 2003. The original fiscal consolidation plan, introduced in 1999, was revised in 2001 and again in 2002. It aimed at reducing the deficit to 2.0 per cent of GDP by 2002 while reaching fiscal balance by 2005. However, lower growth in 2002 brought the budget shortfall to 4.6 per cent of GDP, instead of a previously planned 2.6 per cent. For 2003 further slippage occurred, linked to continued modest growth and tax avoidance with marked revenue shortfalls, while spending increased through higher defence outlays and expansionary measures introduced to offset subdued external demand. This effectively rendered the consolidation program defunct, and the government deficit for 2003 reached 6.3 per cent of GDP. The expansionary fiscal stance contributed to an increase of domestic demand and to a continued relatively high current account deficit projected at 4.4 per cent of GDP for 2003. The government intends to tackle anew the fiscal deficit, thus working towards a more favourable policy mix and supporting a narrowing of the current account deficit. To put fiscal consolidation on track again significant corrective measures are

required. The quality of public finances should improve due to a comprehensive fiscal reform, to be finished by end-2004. These reforms will support further deficit reductions and assist in keeping the current account deficit in sustainable territory if private net saving should become less favourable again.

Increase the diversification of the economy towards higher value added activities

While tourism accounts for around 15-20 per cent of GDP and employment, the economy has shown some resilience in the face of a difficult international environment. However, in a longer term perspective, Cyprus may have an interest to up-grade tourism activities and to develop other value added activities. In this respect, the Cypriot government has initiated a number of reforms to facilitate the transition towards a knowledge based economy. Nevertheless the low level of R&D expenditure, particularly by the business sector, and the lack of IT related skills may still be handicaps. Finally, both e-commerce and the percentage of households with internet access are quite limited.

A better business environment is also key to improving the efficiency of product markets. First, the Cypriot economy is dominated by small family enterprises whose expansion may be partly hindered by access to finance. Second, competition in the network industries is still limited. For example, the unbundling of the transmission system operator is still lacking in the electricity market. In November 2003, the regulator for the telecommunications and postal services sectors issued two decrees advancing but not completing the unbundling of the local loop in these sectors. Finally, barriers to market access remain in air transport and the *acquis* in the maritime sector still has to be fully implemented.

Country specific recommendations to Cyprus

Meeting the challenges outlined above requires broad structural reforms as they are laid down in the general guidelines (GL) in Part I of the Broad Economic Policy Guidelines.

In order to ensure a reduction of the general government deficit on a sustainable basis, Cyprus is recommended to:

1. reduce the general government deficit in a credible and sustainable way within a multi-annual framework in line with the decisions to be taken by the Council in the context of the forthcoming budgetary surveillance exercise (GL 1).

In order to increase the diversification of the economy towards higher value added activities, Cyprus is recommended to:

2. step up efforts to increase the adequacy of skilled human capital, promote R&D and innovation, in particular in the business sector, and improve conditions to facilitate ICT diffusion (GL 9, 13).
3. continue to simplify the business and taxation environment (GL 11).

17. Ir-Repubblika Ċeka

After the economic slowdown of 1997-1998, the Czech Republic's annual real GDP growth averaged about 3 per cent, with the exception of 2002 when the country was hit by serious floods and GDP growth reached only 2 per cent. The HICP inflation reached very low levels (1.4 per cent in 2002 and -0.1 per cent in 2003) and the monetary authorities were undershooting the inflation target. The growth performance has been underpinned by restructuring efforts, but output has not yet fully reached its estimated potential. The main restructuring process took place in the banking sector. The restructuring of the banking sector was accompanied by substantial fiscal costs as the state took over bad assets in the banks' balance sheets. Moreover, fiscal policy has been until recently somewhat relaxed, causing the general government deficit to surge. The expansionary fiscal stance contributed to a domestic demand boom and an increasingly consumption-driven widening of the current account deficit to more than 6 per cent of GDP.

Policies in the Czech Republic should aim at achieving a high degree of sustainable convergence, in particular as regards the consolidation of public finances. The economy has been characterised by relatively low growth in comparison with the other new Member States. Therefore, the further consolidation of public finances needs to be supported by policies which assist in accelerating the growth performance into the medium and long term. This requires, in particular, an effort to tackle the remaining structural shortcomings, notably in the labour market and in the business environment, and to speed up the transition towards a knowledge-based economy. Against this background, the Czech Republic faces four major challenges:

- Urgently ensure a further reduction of the general government deficit on a sustainable basis and the long-term sustainability of public finances,
- Continue to address the structural problems in the labour market,
- Improve conditions for an accelerated productivity growth,
- Promote entrepreneurship and SMEs.

Urgently ensure a further reduction of the general government deficit on a sustainable basis and the long-term sustainability of public finances

The general government deficit increased from 6.4 per cent of GDP in 2002 to 12.9 per cent of GDP in 2003⁶, thereby giving impetus for further worsening of the current account deficit. In 2003, the government has introduced a fiscal consolidation programme which aims to reduce the general government deficit to 4 per cent of GDP in 2006. The fiscal consolidation will support further deficit reductions and assist in bringing the current account deficit in more sustainable territory if private net saving should become less favourable.

However, improvement in the quality of public finances will largely depend on the implementation of the fiscal reform. A very important feature of the fiscal reform is the modification of the institutional framework, with the introduction of the medium-term expenditure frameworks and performance-oriented budgets. In particular, the expenditure frameworks should diminish the central government's incentives to provide state guarantees, which remain a source of substantial fiscal risk. In addition, given the ongoing decentralisation of public administration, the lack of budgetary rules at regional and local levels represents a risk to a sound fiscal position in the future. As a positive development, it is worth mentioning that in its reform plans the government does not foresee a lowering of the share of public investment expenditures as a percentage of GDP in the coming years.

⁶ This deficit is partly due to one single imputed state guarantee, which is about 6.3 per cent of PGD.

As far as the long-term sustainability of public finances is concerned, extra-budgetary spending and rapidly increasing social security and health care expenditures are reasons for major concern. Although the current level of government debt in the country is not high, developments regarding the items above contributed to a rapid increase in recent years (from 25.2 per cent of GDP in 2001 to 37.6 per cent of GDP in 2003).

Continue to address the structural problems in the labour market

Between 1990 and 2002 the Czech labour market experienced substantial structural changes. The share of people employed in the primary sector fell from 12.4 per cent to 4.8 per cent of the labour force, from 45.1 per cent to 39.6 per cent in the secondary sector and increased from 42.5 per cent to 55.6 per cent in the tertiary sector. The unemployment rate was 7.3 per cent at the end of 2002, and has since risen up to 8.1 per cent in the fourth quarter of 2003. In addition to the restructuring process, unemployment is likely to be affected by public finance reform, according to which 2 per cent of public sector jobs are to be lost annually over the period 2004-2006. The impact of trade unions on wage formation is low. The wage negotiation process is decentralised with wage setting mostly at the enterprise level. Bargaining coordination across firms and sectors is weak. Despite the fact that the employment rate is high (65.5 per cent in 2002) and the unemployment rate is around the EU average, the Czech labour market displays a number of structural shortcomings. First, regional disparities in unemployment are very high. The rate of unemployment in structurally weak regions is more than four times higher than in Prague and in some regions it exceeds 25 per cent. Second, the share of long-term unemployed (more than one year) is very high as it reached 40.3 per cent by the end of 2003. In addition, the average period of registration at the labour offices is becoming longer. Third, the rate of youth unemployment (people under 25 years old) is very high. The average share of youth unemployed was almost 23 per cent with substantial regional disparities.

On the labour supply side, long-term unemployment and low occupational flexibility stem from the disincentives embedded in the tax and benefit system, from the underdeveloped system of life-long learning programmes, and from shortcomings of the education and training systems. As regards the latter, they do not sufficiently provide skills that are adapted to the needs of the labour market, in particular to the demands of the knowledge-based economy. The structural shortcomings in the Czech labour market also mirror low geographical mobility, which results from two principal shortcomings: First, the regulation of housing prices weakens incentives for supply of housing in regions where jobs are created. And second, the weak transport infrastructure increases the costs of commuting and creates obstacles for investment and setting up of new enterprises in the structurally weak regions.

On the labour demand side, the high rate of health and social security contributions might have negative effects. The total rate of health and social security contributions has reached 47.5 per cent of gross wage of which about $\frac{1}{4}$ is paid by employees and about $\frac{3}{4}$ by employers.

Improve conditions for an accelerated productivity growth

Productivity growth in the Czech Republic has been comparatively low. Over the period 1996-2002, labour productivity grew by 2.1 per cent annually, the lowest rate among the new members. Moreover, the level of productivity is still very low in comparison with the EU (around 55 per cent of the EU 15 average in 2003). Factors contributing to this situation could be the limited flexibility of the education system, the low effectiveness of R&D and innovation, and the low use of ICT. The limited flexibility of the education and training system in responding to the changing skills requirements manifests itself through the qualification mismatches in the labour market. Educational attainment (the percentage of the population aged 20-24 with at least upper secondary education) is very high (92 per cent), but the share of tertiary graduates is one of the lowest in the EU. Despite a relatively high level of expenditure on R&D in comparison with the new members, the resulting innovation activity, as measured by the number of patents, is very low, pointing to low effectiveness of R&D. There seems to be only limited cooperation between the research institutions (e.g. universities and the Czech Academy of Sciences)

and the private sector. Recognising these problems, the government has adopted the National R&D Policy for 2004-2008 to promote R&D but results will largely depend on its full implementation.

Promote entrepreneurship and SMEs

Despite the progress in establishing a well-functioning competition framework and continuous developments in the legal environment there seem to remain significant barriers to entrepreneurship in the Czech Republic. This is reflected *inter alia* in the low share of GDP accounted for by SMEs (less than 40 per cent). The gross-birth rate of enterprises as a percentage of all enterprises is relatively low in comparison with other new members.

Factors contributing to this situation appear to be the weaknesses in the business environment which have a disproportionately heavier impact on SMEs, e. g. regarding regulations and legal enforcement, excessive administrative burden on companies and limited access to finances. The administrative process of setting up a new company is very lengthy and complicated. The ineffective and often non-transparent operation of the Commercial Register is frequently criticised by entrepreneurs. Also the bankruptcy legislation does not allow for effective market exit or restructuring of troubled companies. Several legislative proposals to tackle some of these problems are currently being prepared but the progress has proven to be slow. Notwithstanding improvements in the qualification of judges, the quality and timeliness of legal enforcement remain fundamental weaknesses. In addition, new businesses find it excessively difficult to find external sources of financing.

Country specific recommendations to the Czech Republic

Meeting the challenges outlined above requires broad structural reforms as they are laid down in the general guidelines (GL) in Part I of the Broad Economic Policy Guidelines.

In order to urgently ensure a further reduction of the general government deficit on a sustainable basis and the long-term sustainability of public finances, the Czech Republic is recommended to:

1. reduce the general government deficit in a credible and sustainable way within a multi-annual framework in line with the decisions to be taken by the Council in the context of the forthcoming budgetary surveillance exercise (GL 1).
2. reform the health care and pension systems to ensure their financial sustainability, in particular to counter the expected increase in the old-age dependency ratio and take measures to reduce fiscal risk stemming from the rising stock of contingent liabilities; and to ensure that incentives to work are enhanced and the high social policy contribution rates are lowered (GL 4, 14 and 16).

In order to continue to address the structural problems in the labour market, the Czech Republic is recommended to:

3. strengthen labour supply by reforming tax benefit systems to eliminate disincentives to work and enhance occupational and regional mobility by reducing skill mismatches, whilst ensuring the efficiency of retraining measures and other active labour market policies, deregulating the housing market, and improving transport infrastructure (GL 4, 7, 8 and 13).

In order to improve conditions for an accelerated productivity growth, the Czech Republic is recommended to:

4. improve the efficiency and quality of the education and training system and its responsiveness to changing skills requirements (GL 13).
5. improve the efficiency of R&D and innovation activities, foster the transfer of knowledge through FDI and support the diffusion of knowledge (GL 13).

In order to promote entrepreneurship and SMEs, the Czech Republic is recommended to:

6. improve the business climate by, in particular, removing administrative burdens, improving and enforcing the legal framework and increasing access to finance (GL 11 and 12).

18. L-Estonja

Against the background of weak external demand, macroeconomic performance in Estonia remained solid in 2003, but the current account deficit widened to 13.7 per cent of GDP. GDP growth of 4.8 per cent was underpinned both by buoyant investment and private consumption growth. The latter was driven by strong credit expansion, higher wages and modest employment growth. Against the backdrop of a protracted investment sluggishness in the euro area, capital spending in Estonia grew briskly at over 11 per cent, due to strong FDI inflows and low interest rates. Inflation, which had accelerated to almost 7 per cent in mid-2001, receded to 1.3 per cent in 2003. The general government surplus widened to 1.8 per cent of GDP in 2002 and further to 2.6 per cent in 2003, on account of strong activity and improved tax collection, and despite additional spending approved by parliament. Some local governments continued to exert a drag on public finances.

Policies in Estonia should aim at achieving a high degree of sustainable convergence, and a narrowing of the current account deficit. Fiscal policy can have a significant impact on the current account, while structural policies, particularly those that aim at improving productivity and increasing competition, can raise the economy's growth potential, and in turn further improve the saving-investment balance and the current account. Additionally, the labour market, and specifically the high unemployment rate, remains an important challenge for the authorities following the restructuring of the economy after independence. Against this background, Estonia faces four major challenges:

- Address the sizeable current account deficit, to which an appropriate fiscal policy should contribute,
- Address the structural problems in the labour market,
- Improve conditions for increasing productivity,
- Develop effective competition in network industries.

Address the sizeable current account deficit, to which an appropriate fiscal policy should contribute

A mismatch between domestic and foreign demand was manifested in a robust demand for imports (7.9 per cent increase), and a relatively sluggish export performance (4.2 per cent increase), and consequently in a deterioration in the current account deficit to 13.7 per cent of GDP in 2003. A number of large one-off items, concerning mainly the import of investment goods, and a negative income balance accounted for a large part of the deficit, while the capital account remained in surplus, thanks to strong FDI inflows. The low level of public debt (around 5 per cent of GDP) and the positive credit rating of the country help to allay immediate stability concerns about the financing of the current account deficit. In addition, the central government has accumulated a “stability reserve” amounting to 9 per cent of GDP, which has been financed from budget surpluses and privatisation revenues since 1997.

Structural policies enhancing the external competitiveness of Estonian goods and services, primarily through a rapid improvement of the country's infrastructure as well as investments in human capital, with a particular focus on the country's disadvantaged regions, are therefore essential to decisively reduce this major macroeconomic imbalance of the Estonian economy in the medium-term.

The continuation of prudent fiscal policies plays a key role in addressing the current account deficit. While the general government surplus increased from 1.8 per cent of GDP in 2002 to 2.6 per cent of GDP in 2003, some local governments continued to exert a drag on public finances with budget slippages in both 2002 and 2003. Despite the fiscal surpluses of recent years and the low public debt, plans for additional expenditures and tax cuts along with commitments related to EU accession will

make for higher budgetary pressure in the near future. This may lower national savings further and thus have a negative impact on the overall policy mix, particularly against the background of a very high current account deficit. On the whole, the Estonian general government balance should remain in balance or in surplus over the next few years, even with some fiscal easing. Moreover, an easing of fiscal policy over the first few years of EU membership is likely to coincide with an economic upswing. A pro-cyclical effect of the envisaged fiscal policy stance may not be ruled out. Thus, the implementation of the medium-term fiscal policy program in Estonia requires a prudent and flexible approach.

Address the structural problems in the labour market

Conditions in the labour market in Estonia have deteriorated gradually following the country's independence. The restructuring of the economy, and the resulting skill mismatch, appear to be the main factors behind the rise in unemployment to 14½ per cent by mid-2000 (based on the ILO definition). The employment rate which had declined from 65 per cent in 1997 to 60.6 per cent in 2000, edged up to 61.1 per cent in 2002 for the first time since the country's independence contributing to a turnaround in the labour market, resulting in a fall in the unemployment rate to 10.3 per cent in 2002. However, this improvement was the result of modest employment gains, and a significant decline in the economically active population; employment increased by some 2 per cent over 1997-2002 while the economically active population declined by almost 2.5 per cent.

The rising unemployment over 1997-2002 was associated with a steady increase in the proportion of long-term unemployed, and of discouraged workers, and consequently an increase in the structural unemployment rate. However, the share of those without a job for more than a year declined to 41 per cent of the unemployed in 2002, or almost to the same level as in 1997, after having increased considerably to 60 per cent during this period. Even so, the number of long-term unemployed remains particularly high, suggesting that a large number of the unemployed do not possess the skills required to reintegrate successfully into the labour market. Regional disparities continue to persist and unemployment remains considerably higher in the Northeast (at around 19 per cent of the labour force) than compared with the South (8½-9 per cent).

Improve conditions for increasing productivity

In Estonia, the level of productivity is still very low compared to the EU average (42 per cent of the EU 15 level in 2002). While labour productivity growth remained strong (7 per cent per annum) over the period 1997-2000, it has slowed down since 2000. Two main factors could constitute a handicap for future increases in productivity growth: the lack of qualifications in the workforce and the low level of R&D and innovation. These two factors also explain that FDI are mainly concentrated in areas that do not require important R&D and qualifications.

The lack of qualifications in the workforce results from inefficiencies in the education system, as public expenditures on education are relatively high (6.7 per cent of GDP in 2000). Particularly worrying is the fact that the education system is not sufficiently close to the needs of the labour market, creating a mismatch.

A well-designed R&D policy can also have an important role in increasing productivity growth. Currently Estonia has a relatively low level of R&D expenditures, below that of other European countries (0.8 per cent of GDP in 2001), and the lowest rate of business R&D among the new members. This is partly due to the weak links between the academic sector and the business community. In this area, a new strategy has been approved which foresees a significant increase in total R&D expenditures over the period 2002-2006.

Develop effective competition in network industries

While the liberalisation of network industries has started in Estonia, competition is still very limited in the electricity market. The country has negotiated a long transition period for the liberalisation of this sector, in light of its dependence on oil shale as a source of electricity generation. The restructuring of the oil-shale sector has started, but the progress made in the planned liberalisation of the market is limited. The electricity market is dominated by a State-owned, vertically integrated company with operations in supply, generation, monopoly transmission and distribution. The declared current market opening of 10 per cent, is below most of the other new member states' degree of market opening. One of the most important obstacles to liberalisation of the electricity market is the imposition of strict import licence rules by the authorities. Ensuring the independence of the energy regulator is also important given the State's ownership of the incumbent in the electricity market.

The problems are less acute in gas and telecommunication. The gas market is privatised and open, with a single supplier operating on the market. The telecommunication market has been also liberalised. However, some problems might arise because the owner of the network also operates as a distributor.

Country specific recommendations for Estonia

Meeting the challenges outlined above requires broad structural reforms as they are laid down in the general guidelines (GL) in Part I of the Broad Economic Policy Guidelines.

In order to address the sizeable current account deficit, to which an appropriate fiscal policy should contribute, Estonia is recommended to:

1. implement a fiscal policy that is in line with the decisions to be taken by the Council in the context of the forthcoming budgetary surveillance exercise (GL 1), and which is consistent with the objective of avoiding pro-cyclical policies that may exacerbate the external imbalance (GL 2).

In order to address the structural problems in the labour market, Estonia is recommended to:

2. adopt policies with particular emphasis on re-integrating the long-term unemployed, particularly in regions worst hit by the restructuring of the economy, by promoting vocational training and life-long learning, and by setting up an effective institutional framework that is supporting job creation (GLs 4, 6 and 8).
3. encourage social partners to ensure that wage developments—including changes to the minimum wage legislation—do not hinder employment growth, and hold up the recovery in the labour market (GL 3 and 5).

In order to improve conditions for increasing productivity, Estonia is recommended to:

4. improve the efficiency and quality of the education system and vocational training in order to reduce the mismatch on the labour market (GL 13).
5. implement the R&D strategy approved in 2001 and, in particular, promote the stronger involvement of the business sector in R&D spending (GL 13).

In order to develop effective competition in network industries:

6. proceed with the liberalisation of the electricity market, strengthen the independence of the regulator and ensure effective competition in telecommunications (GL 9).

19. L-Ungerija

Following a relatively high real GDP growth of 3.5 per cent in 2002, real GDP growth in 2003 slowed to below 3 per cent. While unemployment is among the lowest of the acceding countries, the participation rate is very low compared to the EU average. Serious structural shortcomings in the labour market render further increase in employment difficult: notably a lack of regional mobility, skill mismatches and disincentives from the benefit systems. Achieving a high degree of sustainable convergence requires regaining and maintaining competitiveness at a sustainable high level. A return to reasonable real wage development and the creation of a more investment-promoting environment seems therefore crucial in order to ensure a balanced medium-term growth.

After the high fiscal deficit of 9.3 per cent of GDP in 2002, fiscal policy became restrictive again in 2003. However, the general government deficit still reached 5.9 per cent of GDP. The significant overshooting of the fiscal deficit targets during the last two years contributed to the consumption-driven widening of the current account deficit to above 5 ½ per cent of GDP. Together with other problems in the macroeconomic policy mix (such as the high real wage growth and very high real interest rates) and the high volatility of the exchange rate, this has led to a general loss in financial markets' confidence and to a loss in overall competitiveness.

Policies in Hungary should aim at achieving a high degree of sustainable convergence, in particular as regards the consolidation of public finances. Hungary implemented a number of structural reforms and has achieved important catch-up with the EU. However there are areas which pose further challenges to the country. Hungary should aim to adopt measures in order to make the education system more effective and R&D has to be encouraged in order to achieve higher productivity. Competition in the network industries needs to be further improved and the independence of the regulators has to be strengthened. Against this background, Hungary faces five major challenges:

- Ensure a further reduction of the general government deficit on a sustainable basis,
- Increase employment rates and address the structural problems in the labour market,
- Enhance cost-competitiveness by pursuing policies that induce wage moderation,
- Improve conditions for increasing productivity,
- Develop effective competition in network industries.

Ensure a further reduction of the general government deficit on a sustainable basis

After the high deficit of 9.3 per cent of GDP in 2002, fiscal policy became restrictive in 2003. However, the general government deficit of 2003 was still 5.9 per cent of GDP. While for 2004 a further reduction of the deficit is foreseen, the starting position for the achievement of the 2004 deficit target seems rather difficult. While initially aiming at comprehensive public finance reforms, a significant number of expenditure items have not been addressed at all in the budget of 2004, and still seem not to have been considered in the consolidation plans. Meanwhile, savings are intended to result mainly from cuts in current and operational expenses. The previous expansionary fiscal stance, along with high real wage growth, contributed to high domestic demand and an increasingly consumption-driven widening of the current account deficit, to somewhat above 5½ per cent of GDP. A reduction in the high government sector level of borrowing is also crucial in order to improve the current account. Households' savings can not be expected to be sufficient to finance the rise in private investment (including those related to EU accession). This is expected to put further pressure on the current account. Even maintaining the present current account deficit, while allowing investment to take place, would thus require additional budgetary constraint. A return to sustainable policies in Hungary has to be based on a consolidation of public finances.

Increase employment rates and address the structural problems in the labour market

Hungary has one of the lowest unemployment rates among the acceding countries (5.8 per cent in 2003). However, this is accompanied by a stagnating labour force and a low participation rate (59.7 per cent in the 15-64-year age-bracket for 2002) compared to the EU average. Consequently, the low unemployment rate does not reflect the substantial disengagement from the labour market and the high level of inactivity particularly in the end-of career working age population.

The labour market is also characterised by structural shortcomings. Regional differences can mostly be observed in the form of increasing urbanisation and the East-West axis, with a less developed infrastructure and higher unemployment in the Eastern part of the country. Internal mobility is low in international comparison, with housing and transport as the main impediments. Furthermore, a significant number of unemployed are young adults (the youth unemployment rate is 11.4 per cent).

Enhance cost-competitiveness by pursuing policies that induce wage moderation

While showing a slight improvement since the beginning of 2003, Hungary's cost competitiveness has shown a significant deterioration in the years 2000-2002. The decline in cost competitiveness was partly due to the fast increase in wages. Real wage growth exceeded productivity growth in the last three years, led by a rise in minimum wages and by the public sector, but also by a delayed adaptation of the corporate sector to the new low-inflation environment. Although wage growth slowed down towards the end of the year, real wages still grew by 9.2 per cent in 2003 (with 7.3 per cent in the business sector and 12.7 per cent in the public sector). They have negatively influenced cost-competitiveness, and led to decreasing employment in some low-skill segments of the labour market. While this process has contributed to a change in the structure of industrial production towards high skilled labour, increasing unit labour costs have led to a deterioration in the overall competitive position of the country, not just in labour-intensive activities.

Improve conditions for increasing productivity

Productivity growth has been decreasing since 2000, although it remained slightly above the average of the new Member States. While labour productivity growth was 4.2 per cent in 2000 it decreased to 2.4 per cent in 2003. Factors contributing to the slowdown in productivity growth have been the relatively low level of R&D (0.95 per cent of GDP in 2001), inefficiencies in the education system, and instability in the business environment.

While some measures have been taken to improve the flexibility of the education system in order to better adapt to the changing needs of the labour market, there is still a lack of "middle-skilled" and high-skilled workers in the labour market. The number of PhD students is increasing but many terminate their studies before obtaining their diploma. The number of total tertiary graduates in science and technology per 1000 of population (aged 20-29) has been decreasing during the last years: in 2001 it was 3.7 which is one of the lowest in the EU. In the field of research and development, applied research is lagging behind, partly due to the low level of business R&D expenditures and limited cooperation between companies and research institutes. Public R&D expenditures are also relatively low, not only as a share of GDP but also as a share of total government expenditures (R&D expenditures by the government represented 0.9 per cent of total government expenditures in 2001). Another factor which might negatively affect productivity growth is the frequently shifting policy environment. Regulations and government strategies have often been changed during the last decade, which reduced the predictability of policies and trust in the government, and hampered longer term planning.

Develop effective competition in network industries

While liberalisation has started in most of the network industries, effective competition is still limited in these sectors. One of the most liberalised markets is telecommunication. However, even in this

market, competition is restricted due to the strong dominant position of the previously State owned enterprise in the fixed line market and the quasi duopoly situation on the mobile market. Electricity and gas markets have been opened up for big customers. However, long-term purchase agreements and the low availability of interconnection capacities continue to pose obstacles to competition in electricity. Finally, in certain of these sectors the State has retained its capabilities to intervene in the activities of the network regulators. This is the case in the electricity and gas markets where the government has the possibility to influence prices.

Country specific recommendations to Hungary

Meeting the challenges outlined above requires broad structural reforms as they are laid down in the general guidelines (GL) in Part I of the Broad Economic Policy Guidelines.

In order to ensure a further reduction of the general government deficit on a sustainable basis, Hungary is recommended to:

1. reduce the general government deficit in a credible and sustainable way within a multi-annual framework in line with the decisions to be taken by the Council in the context of the forthcoming budgetary surveillance exercise (GL 1).

In order to increase employment rates and to address the structural problems in the labour market, Hungary is recommended to:

2. strengthen labour supply by removing obstacles to regional mobility through appropriate measures in the housing and transportation policy, and by encouraging disadvantaged groups (ethnic minorities, disabled and homeless people) to (re-)enter the labour market (GL 7 and 8).
3. ensure that the tax and benefit systems support employment and provide incentives to enter or remain in the labour market (make work pay- principle) – the high tax burden of labour force should be further reduced (GL 4).

In order to enhance cost-competitiveness by pursuing policies that induce wage moderation, Hungary is recommended to:

4. encourage a reform of wage setting which allows wages to better reflect productivity. Promote multi-annual wage agreements with the social partners in order to keep real wage development in line with productivity growth (GL 5).

In order to improve conditions for increasing productivity, Hungary is recommended to:

5. promote the stronger involvement of the private sector in R&D and innovation, strengthen the link between business and research institutions, ensure sufficient resources to improve the quality of research and support the transfer of knowledge through FDI (GL 13).
6. improve the efficiency of the education system, increase its flexibility in order to better adapt to the skill needs of the market and ensure adequate resources for vocational training and education (GL 13).
7. ensure stability of legislation and government policies to create a business environment, more supportive to entrepreneurship (GL 11).

In order to develop effective competition in network industries, Hungary is recommended to:

8. proceed with the liberalisation of the network industries, increase effectiveness of competition and the independence of the network regulators (GL 9).

20. II-Latvija

Robust economic performance was registered in Latvia in recent years despite a weak external environment. It is expected that GDP growth will remain at potential growth of 5-6 per cent per year in the medium term. Private consumption and gross fixed capital formation have been particularly strong and are the driving factors for growth. Despite high private consumption growth, inflation remained modest. External trade has expanded rapidly and since imports are outpacing exports, the current account deficit has increased to 9.3 per cent of GDP in 2003 and is expected to remain at this high level in the medium term. Latvia made remarkable progress implementing structural reforms in recent years, but still faces some challenges, that if not fully met, may impair its ability to stay on a path of strong growth.

The unemployment rate declined slowly and varies considerably across regions. The smooth functioning of the labour market is hampered by a number of structural problems, including inadequate education and training systems, skills mismatches and low geographical mobility. Competition on Latvian product markets has been boosted by the privatisation of most State-owned companies, and the level of State aid remains lower than the EU average. The few remaining competition problems are mainly concentrated in network industries. Although Latvia benefits from low labour costs and taxes, the low level of labour productivity remains a major concern.

The decreasing trend in the general government deficit was interrupted in 2002, when it rose to 3 per cent of GDP, from 1.6 per cent in 2001. In 2003 better than expected tax revenues and close monitoring of expenditure by the government helped to reduce the general government deficit to 1.8 per cent of GDP and in 2004 the deficit is planned to be 2 per cent of GDP. However, Latvia's fiscal position depends on the strength of the commitment to ensure budgetary discipline; consequently, a pro-cyclical stance characterizes Latvia's fiscal policy. On the other hand, the general government debt remains low at 15.6 per cent of GDP.

Policies in Latvia should aim at achieving a high degree of sustainable convergence, in particular as regards the consolidation of public finances. Both the further consolidation of public finances and solutions to address the under-utilisation of Latvia's human resources need to be supported by policies which assist in perpetuating the strong growth performance into the medium and long term. This requires in particular a strengthening and diversification of the growth and employment base by fostering the entrepreneurial climate. Furthermore, the productivity level needs to be raised and Latvia should prepare for the eventual transition to a knowledge-based economy. Against this background, Latvia faces four major challenges:

- Address the sizeable current account deficit, to which an appropriate fiscal policy should contribute,
- Improve conditions for increasing productivity,
- Address the structural problems in the labour market,
- Develop effective competition in network industries.

Address the sizeable current account deficit, to which an appropriate fiscal policy should contribute

Latvian domestic demand for imported goods remains stronger than the external demand for Latvian goods, thus, the current account deficit has increased to 9.3 per cent of GDP in 2003. Export growth in 2002 and 2003 was very strong despite the international slowdown; however, imports grew even faster than exports. In the next few years the trade balance is expected to worsen even more, because of strong and growing investment needs as the economy continues to develop and restructure. This will

lead to a broadening of the current account deficit. Although export prices grew faster than import prices in 2003, the terms of trade do not show consistently favourable developments over the last years, thus adding uncertainty regarding potential future pressures on the current account.

The modest pace of fiscal consolidation was disrupted by fiscal slippage in 2002, despite strong economic growth of the Latvian economy. Consequently, the general government fiscal deficit rose to 3 per cent of GDP. Even though the Latvian authorities maintain a commitment to balancing the budget in the medium term, the current pro-cyclical fiscal stance, and a limited ability of the government to increase tax revenues in a period of high economic growth, put Latvia in a difficult position from which to meet future spending needs related to EU and NATO accession. These spending pressures are also likely to exacerbate the current account deficit. In the face of a weak external demand and already high domestic demand, a spending surge in late 2002, strong credit growth, significant tax reduction in early 2003, and further fiscal loosening are a cause for concern. The key economic policy challenge is to avoid a pro-cyclical fiscal stimulus that could overheat domestic demand and aggravate the current account deficit.

Improve conditions for increasing productivity

Labour productivity in Latvia is the lowest in the EU (under 40 per cent of the EU-15 average). Over the period 1995-2003, it has increased relatively to the EU average but its growth rate slowed down in recent years. Several factors bear on Latvia's productivity performance. First, although reforms have been initiated, the educational system still suffers from efficiency, contents, and external partnerships problems, and the links between higher education and industries are still underdeveloped. Second, R&D – in particular the share of business R&D - and innovation activities appear to be limited, both because of a lack of funding and the absence of critical mass for most Latvian companies to carry out research activities. Productivity growth is also constrained by the low level of entrepreneurial activity as companies face heavy local regulations, difficulties in accessing finance, and a nascent entrepreneurial culture. Despite high levels of business investments, productivity levels are still held back by low capital deepening and a still relatively low level of physical infrastructure. All these factors also contribute to explain why Latvia remains specialised in relatively low-tech sectors and in transit activities without much value-added.

Address the structural problems in the labour market

The Latvian labour market displays a number of structural shortcomings, the main being high regional differences in unemployment, and a high share of long-term unemployment and youth unemployment. In 2002, the participation rate reached 68.8 per cent and the employment rate was 60.5 per cent. The unemployment rate was 12.1 per cent at the end of 2002 and has declined in 2003.

The smooth functioning of the labour market is hampered by a number of structural problems. First, the under-utilisation of human resources stems from feeble entrepreneurial climate. Latvia has the lowest rate of business start-ups in the EU, which underlines the necessity to facilitate entrepreneurship and the development of small and medium size enterprises, in this way fostering the employment base. Second, the labour tax wedge is high in Latvia and creates a disincentive to work in the official economy. In addition, given the low wages, even modest social benefits make working or returning to work costly decisions and therefore discourage labour market participation. Third, the high rate of unemployment reflects to some extent skills mismatches between labour supply and demand. Moreover, the education system fails to meet the demand for more flexible and modern forms of training. The Latvian authorities have recently proposed a comprehensive reform of the education system to better adapt it to the requirements of a market economy, however, implementation of the reform might be both costly and lengthy. Finally, regional discrepancies in employment and unemployment are also the result of low geographical mobility, which could be enhanced through improvements in transport infrastructure.

Develop effective competition in network industries.

Steps to liberalise network industries have only been recently taken place with full liberalisation of voice telecommunications in 2003 and progressive liberalisation of other network industries to comply with EU legislation. All network industries are still dominated by the respective incumbents - some of them being gradually privatised – facing low effective competition and benefiting from the absence of a real choice of supplier. Low effective competition has several sources. In some cases, technical and practical barriers impede competition to develop, as is the case in telecommunications, where local loop unbundling, carrier selection and number portability are trailing behind. In some other cases, the legal base for more effective competition is not yet fully in place, such as in energy. One additional source of low effective competition is a lack of interconnection. Latvia's railways connections are not well-developed with Baltic neighbours and other European countries. In gas, the Latvian market is still dominated upstream by very few importers and is *de facto* dependent on Russian gas supply. Finally, cross-border interconnections in electricity between Baltic States and other Member States may be insufficient to cope with long-term demand.

Country specific recommendations to Latvia

Meeting the challenges outlined above requires broad structural reforms as they are laid down in the general guidelines (GL) in Part I of the Broad Economic Policy Guidelines.

In order to address the sizable current account deficit, to which an appropriate fiscal policy should contribute, Latvia is recommended to:

1. reduce the general government deficit in a credible and sustainable way within a multi-annual framework in line with the decisions to be taken by the Council in the context of the forthcoming budgetary surveillance exercise (GL 1 and 2).

In order to improve conditions for increasing productivity, Latvia is recommended to:

2. increase the efficiency, quality and accessibility of the education and training systems, and their responsiveness to the labour markets' needs (GL 13 and 14).
3. encourage R&D and innovation, in particular in the business sector (GL 13 and 14).
4. encourage an entrepreneurial culture (GL 11).

In order to address the structural problems in the labour market, Latvia is recommended to:

5. revise the tax and benefit system in order to make work pay more, in particular by increasing the efficiency of social spending (GL 4).
6. strengthen labour supply by pursuing efforts to better adapt the qualifications of the workforce to the requirements of the labour market and by facilitating labour mobility, especially through improvements in transport infrastructure (GL 7 and 13).

In order to develop effective competition in network industries, Latvia is recommended to:

7. take legal measures to enhance effective competition in network industries and to strengthen the role of the regulator (GL 9).
8. increase physical interconnections with other European networks (GL 9).

21. II-Litwanja

In spite of a weak external environment, Lithuania's macroeconomic performance remained particularly strong in the last two years. Real GDP growth accelerated rapidly to 8.9 per cent in 2003, primarily supported by strong investment and private consumption, although export growth remained robust. A large nominal effective appreciation of the litas, together with strong productivity growth that attenuated wage inflation, led to a decline in price levels. The decline (measured in HICP) amounted to 1.1 per cent in 2003. Strong economic growth was positively reflected in the labour market, although high unemployment remains as a major weakness in the Lithuanian economy.

The decreasing trend in the general government deficit initiated in 2000 was interrupted in 2003, when the deficit increased slightly to 1.7 per cent of GDP, from 1.4 per cent in 2002. Significant increases in both current and capital expenditure, partly associated with EU accession related expenditure, are approved in the budget for 2004 and are expected to result in a further rise of the deficit. Fiscal consolidation is expected to resume in 2005. Moderate budget deficits in previous years have contributed to maintaining sustainable current account deficits, which have to a large extent been financed by foreign direct investment. The currency board arrangement has proved a successful nominal anchor for monetary policy, contributing to macroeconomic stabilisation and historically low inflation rates. The enhanced macroeconomic stability has allowed for a decreasing trend in interest rates in the last few years, contributing to high domestic credit growth and consequently to rapid growth of investment and consumption.

Policies in Lithuania should aim at achieving a high degree of sustainable convergence. The labour market is a source of concern. Decreasing the high unemployment rate and a further consolidation of public finances will be crucial to enhance macroeconomic stability in the medium term. Preserving Lithuania's competitiveness will be of paramount importance for a rapid and sustained convergence with the EU economies. Further structural changes will be necessary to maintain the current productivity growth trend, which is required to close the substantial productivity gap between Lithuania and the EU average. In this regard, adapting the education system to the needs of the labour market and developing R&D and innovation are required to facilitate much-needed progress towards the transition to the knowledge-based economy. Against this background, Lithuania faces four major challenges:

- Address the structural problems in the labour market,
- Maintain low general government deficits,
- Improve conditions for increasing productivity,
- Develop effective competition in network industries.

Address the structural problems in the labour market

Despite visible improvements in the labour market in the last two years, the unemployment rate remained high at 12.7 per cent in 2003 and major structural weaknesses persist. Large regional disparities are evident, with several regions recording unemployment rates around 20 per cent. The youth unemployment rate remained high at 23 per cent in 2002, whereas the long-term unemployment rate stood at 7 per cent. Close to 17 per cent of employment lies in the low-productivity agricultural sector, where significant labour shedding is likely to take place and exert upward pressure on unemployment in the next years.

Major structural shortcomings in the labour market are related to the limited occupational and geographic mobility of the workforce, mismatches between supply and demand of skills and education deficiencies. Despite enjoying high participation rates in higher education, professional qualifications of the Lithuanian workforce are often specialised in areas that do not match properly the current

demand for skills. Labour shortages are emerging in the areas of information technologies, management and several categories of engineering. Enhancing the links between educational institutions and business would help to better adapt vocational training and tertiary education to the current needs. At the same time, lifelong learning activities, which are essential to increase the workforce's capacity to adapt to future demands, are currently at one of the lowest levels among the acceding countries. Further efforts to improve the quality and availability of vocational training would be beneficial, especially in the least developed regions. The high share of low-qualified workers in unemployment calls for special attention to training activities for this category of workers. Improving the educational infrastructure, particularly in poorer regions, would contribute to establishing better framework conditions for attracting investment and increase the workforce's capacity and willingness to move. Further efforts to improve the business environment would help to create employment and offset redundancies stemming from industrial and agricultural restructuring. The unemployment benefits system needs to be streamlined, the size of unemployment benefits are not linked to previous wages, coverage of the insurance is not clearly defined in the legislation and the links between the contributions and benefits of the unemployment insurance system are unclear.

Maintain low general government deficits

The authorities have held to their fiscal consolidation plans. Accordingly, the general government deficit decreased from 5.7 per cent of GDP in 1999 to 1.4 per cent in 2002. However, the deficit reversed its decreasing trend and picked up slightly to 1.7 per cent in 2003. Against the background of higher revenue collection than expected in the first half of 2003, the government decided to allocate additional expenditure by means of a supplementary budget in July 2003. The amendments resulted in significant increases in current expenditure that prevented a further reduction of the deficit in 2003, mainly in the form of compensations for the loss of rouble savings⁷ (about 0.4 per cent of GDP) and agricultural subsidies (0.2 per cent of GDP). The 2004 budget foresees a further increase of the deficit, largely related to a surge in public investment and higher expenditure related to the social security system and public sector wages, as well as significant transition costs of the pension reform. Spending pressures stemming from high investment needs and sizeable fiscal obligations and contingent liabilities denote a risk for the consolidation of public finances in the medium-term.

Despite efforts made to improve the tax system, there is considerable room for improvement as regards the efficiency of tax collection. Government revenues as a percentage of GDP have decreased from 38.1 per cent in 1998 to 33.8 per cent in 2002, while expenditure has remained largely stable. Additional expenditure to the budget plans is frequently allocated in the second half of the year, which prevents a faster consolidation of public finances. A pro-cyclical fiscal policy stance could entail some risks as additional spending pressures are intensifying. Although low budget deficits have contributed to alleviate pressures on the current account in the last years, fiscal policy might need to play a role in mitigating a potential deterioration of the private sector's savings-investment balance, which could be stimulated by the present rapid credit growth dynamics.

Improve conditions for increasing productivity

Lithuania has had high productivity growth after the Russian crisis in 1999, but the productivity level is still very low at 42 per cent of the EU 15 average. Also the recent high productivity growth seems to have been partly caused by one-off effects due to better capacity utilisation of existing resources. With a GDP per capita level at 39 per cent of the EU 15 average in 2002 a high and sustainable productivity growth is necessary to reduce the income gap with the EU. In this respect, deficiencies of the education system and the low level of R&D and innovation are a handicap.

⁷

The government committed to compensate citizens for the loss of rouble savings in the first years of transition and to reconstitute ownership rights or pay pecuniary compensations for real estate property confiscated during Soviet times. The outstanding amounts to be paid accounted for about 6.7 per cent of PGD at the end of 2003.

Firstly, despite high public spending on education and a high number of tertiary graduates there is a mismatch between the skills acquired in the education and training systems and the needs in the business sector as described in the first key challenge. The government is preparing a program for the implementation of an education strategy stretching to 2012, but further efforts may be necessary to adapt the education and training systems to the future needs as the economic structure develops. Secondly, a large share of the current economic structure is based on low technology activities. A change of the structure will require higher R&D and more innovation, which currently are among the lowest in the new Member States. Maintaining high levels of FDI could act as a catalyst through knowledge transfer and thereby contribute to faster structural changes in the economy towards higher value-added sectors and improved productivity. Further development of the physical infrastructure could also contribute to maintaining the high productivity growth. IT expenditure has increased slightly from a very low level and low IT penetration could be a hindering factor for improving productivity.

Develop effective competition in network industries

Despite deregulation in most network industries, effective competition remains weak in all of them, except mobile telephony and road transport. The fixed telephony market was fully liberalised in January 2003, but the incumbent is still the only player in the market. The telephone market regulator does not yet seem to have adequate resources to effectively promote competition. The implementation of the EU legislation on railway market opening has not yet been completed and the infrastructure is poorly developed, especially the interconnections with Poland.

The opening-up of the energy markets have led to few visible benefits for consumers and high concentration ratios persist, both in supply and distribution. The electricity market was opened-up for large customers in January 2002, corresponding to a fourth of the electricity consumption. Further deregulation is foreseen in steps and a privatisation of electricity distributors is currently underway. However, about 80 percent of all electricity is produced by a nuclear power plant and a lack of interconnection capacity with other acceding countries prevents integration with the EU electricity market. Also the gas market has been liberalised for large customers, corresponding to 80 per cent of consumption. However, there are few independent players in the market and there is no interconnection with the Western European gas network.

Country specific recommendations to Lithuania

Meeting the challenges outlined above requires broad structural reforms as they are laid down in the general guidelines (GL) in Part I of the Broad Economic Policy Guidelines.

In order to address the structural problems in the labour market, Lithuania is recommended to:

1. enhance regional mobility and reduce skill mismatches, whilst ensuring the efficiency of education, retraining measures and other active labour market policies (GL 4, 7 and 8).
2. improve the combined incentive effects of taxes and benefits (GL 4).

In order to maintain low general government deficits, Lithuania is in particular recommended to:

3. pursue low budget deficits in a credible and sustainable way within a multi-annual framework in line with the decisions to be taken by the Council in the context of the forthcoming budgetary surveillance exercise (GL 1).

4. avoid pro-cyclical fiscal policies that prevent a further reduction of the general government deficit, in particular by avoiding budget amendments that allocate additional expenditure in response to higher than expected revenues (GL 2).

In order to improve conditions for increasing productivity, Lithuania is recommended to:

5. improve the efficiency and quality of the education and training systems and their responsiveness to labour market needs (GL 13).
6. promote R&D and innovation, strengthen the links between research institutes and the business sector and support knowledge transfer through FDI and higher IT penetration (GL 13).

In order to develop effective competition in network industries, Lithuania is recommended to:

7. pursue liberalisation and enforce effective competition in energy, telecommunication and railway markets (GL 9).
8. create and improve interconnection capacities with neighbouring EU Member States (GL 9).

22. Malta

In-natura miftuha li dejjem qed tizdied ta' l-ekonomija Maltija, id-dipendenza kbira fuq id-dhul mit-turizmu u d-daqs żgħir tagħha jagħmel l-ekonomija iktar vulnerabbli għall-ekonomija esterna u x-xokkijiet ġeopolitiċi. L-ambjent internazzjonali ekonomiku diffiċli fl-aħhar sentejn u r-ristrutturar tas-settur pubbliku ġab tkabbir ekonomiku limitat, l-aktar minhabba konsum kbir mill-pubbliku. It-tkabbir reali tal-GDP bħalissa hu hafna aktar baxx mill-potenzjal stimat.

Minkejja tkabbir ekonomiku batut, il-qgħad ma żdiedx sostanzjalment fil-perjodu bejn Jannar u Ottubru tas-sena l-oħra (5.7 perċentwali f'Ottubru 2003), għalkemm hi mistennija deterjorazzjoni fix-xhur sussegwenti, marbuta ma' l-istrutturar fl-industrija tat-tarzna u fis-setturi tal-manifattura u t-turizmu. Il-progress ġenerali ta' Malta fl-adozzjoni ta' l-*acquis* ma kienx akkumpanjat mit-tkomplija tar-riformi ekonomiċi kruċjali kontra l-isfond tas-shubija fl-UE f'Mejju 2004. It-tnaqqis fis-settur pubbliku u t-tnaqqis fl-għajjnuna ta' l-Istat u s-sussidji u r-riforma tal-pensjonijiet u s-sistemi tas-saħħa ġew posposti, bir-riżultat ta' impatt neggattiv fuq it-tkabbir ekonomiku, il-holqien ta' l-impjiegi u l-finanzi pubbliċi. Ir-rata ta' qgħad komparabbilment baxxa, partikolarment fost in-nisa, tibqa' haga tat-thassib. Fil-kuntest ta' sforzi żgħar biex jiġu kkonsolidati l-finanzi pubbliċi, tkabbir tal-GDP inqas milli mistenni fis-sena 2003 u n-nefqa pubblika li dejjem qed tizdied iddeterjoraw iżjed l-iżbilanc tal-gvern ġenerali, li jpoġġi pressjoni fuq il-bilanċ tal-kont kurrenti. Il-politika f'Malta għandha tfitteż livell għoli ta' konverġenza sostenibbli, b'mod partikolari fir-rigward tal-konsolidazzjoni tal-finanzi pubbliċi. B'din il-mira f'moħħna, il-pass tar-riforma fil-pensjonijiet u s-sistemi tal-kura tas-saħħa u s-settur pubbliku għandhom jerga' jibda jizdied Minkejja li sar certu progress, il-grad tal-kompetizzjoni f'certi oqsma għadu mhux biżżejjed u l-isforzi tal-privatizzazzjoni jridu jtkomplew. F'dan l-isfond Malta trid thabbat wiċċha ma' tliet sfidi ewlenin:

- Tiżgura tnaqqis ta' l-iżbilanc ġenerali tad-defiċit tal-gvern fuq bażi sostenibbli u sostenibbiltà fit-tul tal-finanzi pubbliċi,
- Żjieda fir-rati ta' l-impjiegi, speċjalment fost in-nisa,
- Thegħgeġ kompetitività effettiva billi tqis il-karatteristiċi speċifiċi ta' ekonomija domestika żgħira.

Tiżgura tnaqqis ta' l-iżbilanc ġenerali tad-defiċit tal-gvern fuq bażi sostenibbli u sostenibbiltà fit-tul tal-finanzi pubbliċi.

Biex jiffaċċja l-figuri għoljin ta' l-iżbilanc fil-baġit ġenerali tal-gvern, il-gvern qed jippjana li jimplementa sensiela ta' miżuri biex isahħaħ l-infurzar tat-taxxa biex iżid id-dhul. Huwa interessanti li wiehed jinnotta li d-dhul mhux mit-taxxa hu mistenni li jikber aktar mid-dhul mit-taxxa. Primarjament dan huwa dovut l-aktar minhabba d-dhul miġbur taħt l-iskema tar-registrazzjoni barranija u minhabba l-Kumpens tal-Baġit ta' l-UE fil-kwadru tal-Pakkett ta' Kopenhagen. Fir-rigward tat-taxxa diretta, xi tnaqqis hu ppjanat minhabba l-introduzzjoni ta' taxxa b' hames kategoriji (s'issa, hemm tliet kategoriji) u ż-żieda fit-*threshold* tad-dhul li għandu jkun intaxxat.

Min-naħa tan-nefqa, il-piżijiet kbar tal-pagi fis-settur pubbliku, il-pensjonijiet u żjieda fin-nefqa fuq is-sistema tas-saħħa huma ta' riskju għas-sostenibbiltà tal-finanzi pubbliċi. Fir-rigward tan-nefqa kurrenti, hemm bżonn ta' kontroll oġhla ta' l-approprijazzjoniet tal-benefiċċji tal-*welfare* u programmi oħra ta' għajjnuna, barra minbarra t-tnaqqis fis-sussidji. Madankollu, minhabba bżonnijiet persistenti għall-immodernizzar u l-bini ta' infrastruttura ġdida, in-nefqa kapitali tista' żżomm n-nefqa globali fl-livell għoli (maqwar 50 perċentwali tal-GDP), għalkemm hu mistenni li jonqos fl-2006 (għal madwar 46.6 perċentwali tal-GDP).

Il-popolazzjoni li dejjem tixjeh tfisser riskju fiskali relativament sinifikanti għas-sostenibbiltà fit-tul tal-finanzi pubbliċi, b'mod partikolari minhabba livell għoli ta' dejn tal-gvern. Iz-żieda mgħaġġla mistennija fir-*ratio* tad-dipendenza ta' l-anzjani bejn is-snin 2000 u 2050 (minn 18% għal 38.6%)

għandha thalli pressjoni fiskali sinifikanti fuq il-finanzi pubblici fil-futur. Filwaqt li riforma fl-ewwel pilastru ta' l-iskema tal-pensjoni qed tiġi pplanata, m'huwiex ċar meta se tkun implimentata.

Il-livell sostenibbli għall-garanziji ta' l-istat li għad baqa' (22 fil-mija ta' -GDP fl-2002) qed thedded il-pożizzjoni fiskali tal-gvern. Il-pjanijiet tal-gvern huma li fil-futur jillimita l-hrug ta' garanziji godda (tnaqqis fl-ammont għal 15% tal-GDP fl-2006), li għandha ssir mill-infurzar strett tar-regoli tal-baġit li jirregolaw il-hrug tal-garanziji. Dan għandu jikkontribwixxi għal tnaqqis ippjanat f' terminu medju fil-livell tad-djun kontingenti impliċiti u jnaqqas ir-riskju eżistenti espost, li jirriżulta mill-hrug ta' ittri ta' konfort jew faċilitajiet tal-krediti.

Jżieda fir-rati ta' l-impjiegi, speċjalment fost in-nisa

F'Malta, is-suq tax-xogħol jidher li hu flessibbli bizzejjed biex jaġġusta għax-xokkijiet ekonomiċi mingħajr ma jiġġenera perjodi twal ta' qgħad għoli. Madankollu, f'Settembru 2003 ir-rata ta' l-impjiegi (53.7%) kienet iktar baxxa meta mqabbla mal-medja ta' l-UE. Ir-rata ta' l-impjiegi relattivament baxxa kienet attribwita għar-rata baxxa ta' impjiegi femminili (33.1 fil-mija) peress illi l-figura ekwivalenti maskili (74.2%) kienet oghla mill-medja ta' l-UE. Iż-żjieda fir-rata totali u fir-rata ta' l-impjieg tan-nisa hi ta' importanza kbira biex titwessa' l-bażi għall-kontribuzzjonijiet tas-sigurtà soċjali, fid-dawl ta' popolazzjoni li dejjem qed tixjeh. F'dan ir-rigward, dan l-aħħar ittiehdu xi miżuri li jinkoragixxu l-partecipazzjoni femminili, għax il-preżenza baxxa tan-nisa fis-suq tax-xogħol hi, sa ċertu punt, minhabba fatturi kulturali li jistgħu jingħelbu maz-żmien.

Kif il-gvern jirrealizza l-importanza li tiżdied il-partecipazzjoni femminili fix-xenarju ta' rati tat-twelid li qed jonqsu u popolazzjoni li qed tixjeh, inizjattivi mmirati lejn iż-żjieda fir-rata tal-partecipazzjoni femminili huma inkluzi fl-Att dwar l-Impjiegi u r-Relazzjonijiet Industrijali (ERA), li dahlu fis-sehħ f'Diċembru 2002 u kienu kkumplemetati bi tmien avvizi legali (wiehed minnhom jikkonċerna r-Regolament dwar id-Dritt tal-Leave tal-Ġenituri). Inizjattivi oħrajn f'dan il-qasam huma l-Iskema ta' Childminding, u Pjan ta' Azzjoni dwar l-Ugwaljanza bejn is-Sessi u mainstreaming tas-sessi fis-settur pubbliku. Iżjed minn hekk, it-tlestija tal-proċess tal-privatizzazzjoni u t-tnaqqis fis-settur pubbliku jistgħu jikkontribwixxu lejn riżorsi iktar effiċjenti għall-vantaġġ tas-settur privat u jkun jistgħu jagħtu spinta lill-ekonomija u lill-impjiegi.

Taxxi għoljin fuq il-pagi jfixklu kemm id-domanda kif ukoll il-provvista tax-xogħol, fil-waqt li l-attività tiġi trasferita lejn l-ekonomija informali. Id-differenza bejn il-paga minima u l-benefiċċji tal-qgħad, speċjalment għall-familji kbar, tibqa' baxxa ħafna u tnaqqas l-inċentivi għax-xogħol. Skemi ta' irtirar kmieni użati bħala mezz għar-ristrutturar ta' l-entitajiet tas-settur pubbliku għandhom ikunu limitati wkoll, bl-isforzi jiġu indirizzati lejn it-tahrig mill-ġdid. L-ERA jirregola wkoll l-impjegati part-time u l-kuntratti ta' servizzi għal terminu fissi biex iżid il-fessibilità fis-suq tax-xogħol. L-Attivitajiet Edukattivi Vokazzjonali żdiedu mill-2001, meta gie mwaqqaf il-Kulleġ Malti għall-Arti, Xjenza u Teknoloġija, għalkemm għandhom isiru iktar sforzi biex titjeb ir-rata ta' suċċess fl-edukazzjoni sekondarja u jitnaqqas in-numru ta' dawk li jhallu l-iskola kmieni. Fl-2003 inħolqu tliet istituti godda fl-oqsma tal-Mekkanika, ta' l-Inġinerija, l-Ażjendi Agrikoli u s-Servizzi fil-Komunità. Huwa importanti li wiehed jinnota il-livell eċċezzjonalment għoli tal-kisbiet fl-edukazzjoni sekondarja, u l-livell baxx ħafna miksub fil-livelli sekondarji għoljin u dawk terzjarji.

It-thegġig tal-kompetitività effettiva billi jittiehdu in konsiderazzjoni l-karatteristiċi speċifiċi ta' ekonomija domestika żghira

Numru sinifikanti ta' riformi gew introdotti biex iżidu l-kompetizzjoni fl-ekonomija Maltija. Fl-industriji tan-netwerks, is-settur tat-telekomunikazzjoni huwa issa lliberalizzat, filwaqt li s-settur tas-servizzi postali qed jinfetaħ iżjed. Fit-trasport bl-ajru, il-monopolju ta' l-attivitajiet ta' assistenza fuq l-art (groundhandling) tneħħa wara li harget sejha internazzjonali għall-offerti. Fir-rigward tat-trasport marittimu, l-implimentazzjoni ta' l-acquis għandha trid tiġi kompluta. F'xi setturi ta' l-ekonomija

Maltija, il-kompetizzjoni hija dgħajfa, bħal fit-thin tal-qamh u fiż-żrieragh ta' -likel, u fis-settur tal-bini tal-vapuri, fejn l-għajnuna ta' l-istat għandha titnaqqas flimkien mal-proċess ta' l-istrutturar.

Rakkomandazzjonijiet speċifiċi għal Malta

Biex jintlahqu l-isfidi msemmija hawn fuq hemm bżonn riformi strutturali kif inhuma stabbiliti fil-linji ta' gwida ġenerali (GL) f'Parti I tal-Linji ta' Gwida tal-Politika Ekonomika Wiesa'.

Biex tassigura tnaqqis ta' l-iżbilanc ġenerali tal-gvern fuq bażi sostenibbli u s-sostenibbiltà fit-tul tal-finanzi pubbliċi, Malta qed tingħata l-parir li:

1. tnaqqas l-iżbilanc tal-gvern b'mod kredibbli u sostenibbli fi kwadru multi-anwali fil-linja mad-deċizzjonijiet meħuda mill-kunsill fil-kuntest ta' l-eżerċizzju tas-sorveljanza tal-baġit li jmiss (GL 1).

Biex iżżid r-rati ta' l-impjiegi, speċjalment fost in-nisa, Malta qed tingħata parir sabiex:

2. tirranġa l-interazzjoni tas-sistema tal-benefiċċji fiskali biex issaħħah l-inċentivi għax-xogħol u tnaqqas it-taxxa fuq ix-xogħol sabiex ittejjeb il-kompetitività. (GL 4).
3. ittejjeb il-kwalità ta' l-edukazzjoni sekondarja u t-tahrig vokazzjonali (GL 8).
4. issaħħah it-tahrig mill-ġdid tal-ħaddiema u tagħmilhom iktar flessibbli f'każ ta' bdil tax-xogħol u tiffaċilita r-ritorn lejn id-dinja tax-xogħol ta' nisa ta' età medja (GL 8).

Biex thegġeg il-kompetitività effettiva meta wiehed iqis il-karatteristiċi speċifiċi ta' ekonomija domestika żgħira, Malta qed tingħata l-parir li:

5. tagħmel sforzi biex iżżid il-kompetizzjoni f'ċerti setturi bħal fl-industriji tan-netwerks, l-industriji ta' l-ikel, u t-tarznari (GL 9).

23. II-Polonja

After a record of strong growth during most of the 1990s, Poland experienced a sharp economic slowdown in 2001-2002. Since the end of 2002, the recovery has gradually gained strength, and real GDP growth accelerated to 3.7 per cent in 2003. In 2004, growth is likely to reach its potential level estimated at around 4.5 per cent.

Despite remarkable progress in recent years, Poland still faces serious structural problems that may impair its capacity to stay on a path of strong growth. The unemployment rate has increased rapidly since 1999 and is now, at about 20 per cent, the highest among the acceding countries. In parallel, the employment rate has fallen markedly and almost half of the working age population is without work. The smooth functioning of the labour market is hampered by a number of structural problems, including limited responsiveness of wages to labour conditions, disincentives from the tax and benefit system, skills mismatches and low geographical mobility.

Poland's fiscal position has deteriorated significantly since 2000, as a result of both cyclical factors and the relaxation of fiscal policy. The general government deficit increased from 1.8 per cent of GDP in 2000 to 3.6 per cent in 2002. Until recently, the authorities have shown some reluctance to tackle the fiscal problems, including the rapidly rising debt ratio. The public finance reform adopted by the government early this year envisages substantial spending cuts but postpones the needed fiscal adjustment until 2005.

Policies in Poland should aim at achieving a high degree of sustainable convergence, in particular as regards the consolidation of public finances. Moreover, stability-oriented macroeconomic policies need to be complemented by structural reforms aiming at improving Poland's growth performance. In addition to the under-utilisation of human resources, the relatively low productivity level limits the capacity of the Polish economy to increase both actual and potential output growth. To address this issue, continued efforts are needed to improve the education and training system and also to create favourable conditions for R&D and technology transfer. In addition, the economy, in particular the agriculture sector, calls for more restructuring and there is room to improve the business environment. Against this background, the challenges facing Poland are to:

- Urgently address the deep-seated structural problems in the labour market,
- Ensure a reduction of the general government deficit on a sustainable basis and the long-term sustainability of public finances,
- Improve conditions for increasing productivity,
- Speed up the restructuring of the economy and accelerate privatisation in industry,
- Improve the business environment.

Urgently address the deep-seated structural problems in the labour market

Poland has the highest unemployment rate (19.8 per cent in 2002) and the lowest employment rate (51.5 per cent) among the acceding countries. The employment rate is exceptionally low among elderly people and young people. In addition, the Polish labour market displays the following features: a high youth unemployment rate, a high long-term unemployment rate, significant differences across regions and a high share of unemployed in rural areas.

The smooth functioning of the labour market is hampered by a number of structural problems. First, the concentration of unemployment in particular regions and among certain groups reflects in part the imperfect adjustment of wages to regional differences in productivity and individual skill levels. The wage-setting process lacks flexibility and in particular has proved so far ineffective in imposing wage

discipline in state-owned enterprises and in the general government sector. In addition, the nationally-set minimum wage is high relative to average wages in many regions and hence contributes to the persistence of high unemployment among young and low-skilled workers.

Second, the labour tax wedge is high in Poland and creates a disincentive to work in the official economy. In addition, the combined effects of tax and benefit systems make working or returning to work a costly decision and therefore discourage labour market participation. Tightening the eligibility criteria for disability pensions and phasing out early retirement benefits would be a first step towards increasing the attractiveness of work.

Third, the high rate of unemployment reflects to some extent skills mismatches between labour supply and demand. Moreover, education levels in the adult population are relatively low. The Polish authorities have recently launched a comprehensive reform of the education system to better adapt it to the requirements of a market economy. Finally, regional discrepancies in employment and unemployment are also the result of low geographical mobility, which could be enhanced through reforms of the housing market and improvements in transport infrastructure.

Ensure a reduction of the general government deficit on a sustainable basis and the long-term sustainability of public finances

Poland's fiscal position has deteriorated significantly since 2000, only partly for cyclical reasons. The general government deficit reached 3.6 per cent of GDP in 2002 and is estimated to have increased further to 4.1 per cent in 2003. The fiscal expansion over the last two years is to a large extent due to a loosening of the fiscal stance. Fiscal policy is expected to remain pro-cyclical in 2004. The government has recently adopted a public finance reform which provides for savings in social spending and administrative expenditure over the period 2004-2007. However, there remains uncertainty with regard to the approval of the full fiscal reform package by Parliament. Reining in the government deficit is also crucial to maintain the current account deficit at sustainable levels, especially in case the current savings-investment surplus of the private sector should diminish sharply in the coming years.

The deterioration of fiscal accounts together with the slowdown in privatisation has resulted in a sharp increase in the government debt ratio since 2001. Although still relatively low by international standards, the debt level is rapidly rising and approaching the thresholds that trigger corrective mechanisms under the fiscal rules laid down in the Polish Constitution and the Public Finance Act. In view of the government's growing borrowing needs, the exposure of the budget to foreign exchange risk and risks stemming from contingent liabilities, debt dynamics is a major matter of concern.

Contingent liabilities constitute potentially a serious risk to the sustainability of public finances. State-owned companies in the sectors in need of restructuring are an important source of such liabilities. The stock of outstanding guarantees is rapidly increasing and will put pressure on public finances in the coming years.

The demographic structure in Poland is still relatively favourable. Nevertheless, the pension system underwent a major reform in 1999 in order to adjust it to the demographic and labour force changes and to counter the consequences of the expected sharp increase in the old-age dependency ratio (from 18 per cent in 2000 to 50 per cent in 2050).

Improve conditions for increasing productivity

Despite reasonable productivity gains over the period 1995-2002, labour productivity per person employed (in PPS) in Poland was less than half that of the EU15 in 2002 and below the average of the

new Member States. The catching-up process is therefore not satisfactory yet. This relatively low productivity level may be explained by various factors.

First, there is the high share of employment in agriculture, a sector with particularly low productivity levels. The difficulty of new firms to grow and the lack of mobility may be slowing down the transition of workers from agriculture to other activities. Second, Poland remains below the EU15 average in terms of investment in ICT and R&D. The low level of business investment in R&D is particularly problematic (only 30 per cent of the total R&D expenditure is financed by firms). Reasons cited include insufficient cooperation between research establishments and business, a lack of highly-skilled human capital and the fact that for firms short-term financial considerations tend to override long-term interests. An increase in the skills of the workforce is also to be achieved by promoting tertiary education and life-long learning. The low productivity is indeed related to the structural problems in the labour market, particularly a mismatch between skills taught in the education system and those required by the market place, together with a need for investment in physical infrastructure.

Speed up the restructuring of the economy and accelerate privatisation in industry

After a slow start, privatisation peaked in 2000 (as testified by a peak in FDI of 5.7 per cent of GDP which was boosted by a few large one-off privatisation transactions), but it has slowed down again since then, as the most attractive assets have been sold. The traditional sectors remain state-owned (among others mining, chemicals, defence sectors and railway). In these sectors, the Polish government has favoured a policy of consolidation before privatisation with the aim of creating “national champions” able to compete on EU markets. The pressure to limit short-term social disruption and the substantial consultation required with social partners and several ministers slow down the privatisation process. As a result, the attractiveness of firms to be privatised is considerably reduced, often deterring potential investors. Yet, there is evidence that the FDI inflows have contributed to restructuring the manufacturing sector and improved the export capacity and distribution networks. This is partly because, following privatisation, strategic investors have injected substantial equity capital and know-how into their firms which has resulted in large productivity gains.

The liberalisation of the electricity and gas sectors has started. Local and long-distance telecommunication services were fully liberalised in January 2002 and international services since January 2003. However, the level of competition in network industries is not satisfactory. In the gas sector, there is currently no unbundling at all. In telecommunications, the incumbent has retained its dominant position in the market. Prices for international calls are among the highest. Moreover, the Competition Office has repeatedly found the incumbent guilty of using its dominant position to the disadvantage of competitors.

State aid remains high (in form of tax and social security arrears) and state-owned firms have large debts to other companies, damaging those companies’ finances. With respect to the enforcement record, shortcomings have been identified in the handling of rescue and restructuring aid as well as research and development aid.

Improve the business environment

Poland has made substantial progress in developing a large SME sector thanks to recent reforms. In particular, a new enterprise register is being set up, which creates a “one-stop shop” for firms from January 1, 2004. Since January 2004 a single 19 per cent corporate tax is also in application. Finally, a new solvency law was adopted in 2003 bringing the bankruptcy framework in line with the requirements of a modern market economy. The SME sector accounts for around two-thirds of employment and half of GDP and exports in Poland. However, SMEs continue to face difficulties in growing. Despite the recent reforms to support entrepreneurship, the firm size remains small and the

entrepreneurship environment can still be improved. This is due to the lack of human capital, the lack of labour mobility, the underdeveloped infrastructure (especially the road and telecommunication networks), the high tax-burden (social security contributions in particular) and the liquidity constraints. These factors limit company creation and growth. Therefore, there are concerns that the problems just mentioned may reduce Poland's attractiveness to foreign investors (FDI).

Country-specific recommendations to Poland

Meeting the challenges outlined above requires broad structural reforms as they are laid down in the general guidelines (GL) in Part I of the Broad Economic Policy Guidelines.

In order to urgently address the deep-seated structural problems in the labour market, Poland is in particular recommended to:

1. increase the flexibility of the wage-setting process to ensure that wages better reflect differences in productivity across skills, firms and regions (GL 5).
2. lower the tax burden on labour, together with efforts to widen the tax base on labour and to improve the efficiency of the tax collection and enforcement system, and reform the tax and benefit systems to eliminate financial disincentives to work, in particular high inactivity traps for married couples, and to increase the efficiency of social spending (GL 4).
3. strengthen labour supply by pursuing efforts to better adapt the qualifications of the workforce to the requirements of the labour market and by removing obstacles to regional mobility, especially through reforms of the housing market and improvements in transport infrastructure (GL 7 and 13).

In order to ensure a reduction of the general government deficit on a sustainable basis and the long-term sustainability of public finances, Poland is recommended to:

4. reduce the general government deficit in a credible and sustainable way within a multi-annual framework in line with the decisions to be taken by the Council in the context of the forthcoming budgetary surveillance exercise (GL 1 and 2).
5. monitor the reform of the pension system to counter the expected increase in the old-age dependency ratio, and take measures to reduce the fiscal risk stemming from the rising stock of contingent liabilities (GL 15 and 16).

In order to improve conditions for increasing productivity, Poland is recommended to:

6. pursue and reinforce efforts to improve the efficiency and quality of the education and training system and its responsiveness to changing skills requirements (GL 13).
7. promote R&D and innovation, in particular in the business sector, and support the transfer of knowledge through FDI (GL 13).

In order to speed up the restructuring of the economy and accelerate privatisation in industry, Poland is recommended to:

8. reduce the overall level of State aids, whilst reorienting aid towards horizontal objectives (GL 9 and 14).
9. encourage market entry and effective competition in network industries while pursuing a greater connectivity of national markets (GL 9).

In order to improve the business environment, Poland is recommended to:

10. continue reducing administrative burden, simplifying regulation and supporting the growth of SMEs, in particular, by improving access to finance (GL 11).

24. Is-Slovakkja

After a stabilisation-induced slowdown in 1998, Slovakia's real GDP growth has steadily accelerated and exceeded 4 per cent in 2003, for the second year in a row. Nevertheless, output has not yet fully reached its estimated potential.

The growth performance has been underpinned by intensified structural reforms. Prime examples were the restructuring and privatisation in the banking and non-financial sectors. However, this did not come without cost: the unemployment rate ratcheted up to more than 19 per cent in 2001 and still amounts to around 17 per cent. A broad array of structural shortcomings in the labour market – notably a lack of regional mobility, disincentives from the benefit systems, wage inflexibilities, and skill mismatches – have been hampering its re-absorption capacity and are only being tackled now.

Public finance reforms have been very limited until recently as well and the general government deficit surged to more than 7 per cent of GDP in the election year of 2002. The expansionary fiscal stance contributed to a domestic demand boom and an increasingly consumption-driven widening of the current account deficit to more than 8 per cent of GDP. The government in office since 2002 has started to tackle the root causes of the fiscal deficit, thus supporting a significant narrowing of the current account deficit in 2003.

Policies in Slovakia should aim at achieving a high degree of sustainable convergence, in particular as regards the consolidation of public finances. Both the further consolidation of public finances and solutions to the under-utilisation of Slovakia's human resources need to be supported by policies which assist in perpetuating the strong growth performance into the medium and long term. This requires in particular a strengthening and diversification of the growth and employment base by fostering the entrepreneurial climate through an improved legal framework and judicial and administrative capacity building. Furthermore, the productivity level needs to be raised and Slovakia should prepare itself for its eventual transition to a knowledge-based economy. Against this background, Slovakia faces four major challenges:

- Ensure a further reduction of the general government deficit on a sustainable basis,
- Continue to address the deep-seated structural problems in the labour market,
- Improve the business environment and support entrepreneurship,
- Improve conditions for increasing productivity.

Ensure a further reduction of the general government deficit on a sustainable basis

The general government deficit decreased from 7.2 per cent of GDP in 2002 to an estimated 5 per cent of GDP in 2003, thereby supporting a significant narrowing of the current account deficit. The major part of a comprehensive agenda of public finance reforms has already been passed. These reforms will support further deficit reductions and assist in keeping the current account deficit in sustainable territory if private net saving should become less favourable again. The scope and speed of reforms have been remarkable. However, they also lead to non-negligible uncertainties with respect to the budget execution in 2004 and beyond. Risks stem in particular from the fundamental nature of the tax reforms, notably the introduction of a flat income tax rate of 19 per cent for corporates and individuals. These reforms make revenue forecasts relatively uncertain. Uncertainties also remain on the expenditure side, including with respect to further health reform measures. Moreover, a substantial

part of the planned expenditure reduction relies on projected lower interest outlays based on smooth nominal convergence.

Continue to address the deep-seated structural problems in the labour market

Slovakia has one of the lowest employment rates (around 57 per cent) and the second highest unemployment rate (currently around 17 per cent) in the acceding countries. Employment is particularly low in the age group over 55. Unemployment is concentrated among the young (below 24) and the low skilled. Regional disparities are high. The underlying structural deficiencies of the labour market are multi-faceted and are now being addressed more decisively.

Incentives to work and to leave the informal sector are being strengthened by social benefit and pension reforms, including an increase of the retirement age to a still relatively low level of 62. Regional mobility is being enhanced by financial support for commuters and housing benefits but continues to be limited as the transport infrastructure and the functioning of the housing market improve only gradually. Skill mismatches hinder in particular the reintegration of the long-term unemployed, although retraining measures are being intensified. A still low alignment of the education system with the requirements of a market economy contributes to persistent youth unemployment.

Job creation has been fostered by recent amendments to the labour code, which allow more flexible work relationships. However, the wage setting mechanism is not yet flexible enough and does not sufficiently cater for enterprise-specific conditions. In particular, the possibility of administrative extensions of collective wage agreements to enterprises that have not participated in the negotiations runs counter to this goal. In addition, minimum wages may have negative effects on labour demand and may insufficiently reflect local labour market conditions.

Slovakia's far-reaching income tax reform, effective since the beginning of 2004, will strengthen both job creation and the willingness to work. In contrast, the combined health and social contribution rates have only been lowered to a still very high level of almost 48 per cent of gross salary.

Improve the business environment and support entrepreneurship

Over the recent years, the government has introduced a number of measures aimed at improving the business environment. The procedure for setting up a new business has been significantly simplified and shortened. New bankruptcy legislation is being prepared that should replace the current system under which bankruptcy proceedings last excessively long and allow virtually no scope for the restructuring of troubled companies. The business environment was further strengthened by, for example, the substantial acceleration in price liberalisations in 2003 and the introduction of a new collateral law.

Despite these improvements, there still seem to be important barriers to entrepreneurship in Slovakia. The gross-birth rate of new enterprises is relatively low. According to business surveys, the degree of legal uncertainty remains a fundamental weakness. This stems from the often insufficient and unstable legislative framework and, in particular, weak legal enforcement, which frequently suffers from lack of quality, timeliness and transparency.

Improve conditions for increasing productivity

While retaining relatively high labour productivity growth, the level of productivity is still low (around 58 per cent of the EU average in 2003). Factors contributing to this situation are the lack of

flexibility of the education system, coupled with low education expenditures and the weak R&D and innovation activity.

The education system does not seem to respond appropriately to the labour market needs. This is particularly the case for secondary schooling which often produces graduates with obsolete skills. Moreover, the share of tertiary graduates is very low. The high share of long-term unemployed poses an additional challenge for the vocational and training programmes. Furthermore, expenditure on education has dropped to one of the lowest levels among the new Member States in 2001. Responding to these problems, the government has taken first steps towards rationalising the system, improving its efficiency and increasing the sources of financing.

In 2002, the expenditures on R&D accounted for only 0.59 per cent of GDP, less than in most of the acceding countries. Innovation activity, as measured by the number of patent applications, is very low. The government has undertaken some measures to improve the situation regarding R&D (e.g. by improving the legislative framework for R&D), and is committed to increasing the public resources available for R&D support.

Country specific recommendations to Slovakia

Meeting the challenges outlined above requires broad structural reforms as they are laid down in the general guidelines (GL) in Part I of the Broad Economic Policy Guidelines.

In order to ensure a further reduction of the general government deficit on a sustainable basis, Slovakia is recommended to:

1. reduce the general government deficit in a credible and sustainable way within a multi-annual framework in line with the decisions to be taken by the Council in the context of the forthcoming budgetary surveillance exercise (GL 1).

In order to urgently continue to address the deep-seated structural problems in the labour market, Slovakia is in particular recommended to:

2. strengthen labour supply by removing obstacles to regional mobility and by reducing skill mismatches, whilst ensuring the efficiency of retraining measures and other active labour market policies (GL 4, 7 and 8).
3. generate additional labour demand by allowing for more flexibility in the wage setting mechanism (GL 5 and 18).
4. lower the very high combined health and social contribution rates, while observing the overall budgetary consolidation constraints, in particular by additional health system reform measures and by considering additional adjustments in the pay-as-you-go pillar of the pension system, in particular a further increase of the retirement age (GL 4 and 16).

In order to improve the business environment and support entrepreneurship, Slovakia is recommended to:

5. strengthen the legislative framework supportive to entrepreneurship and improve its enforceability by, in particular, adopting the new bankruptcy legislation and increasing the capacity and transparency of the judicial system (GL 11 and 12).

In order to improve conditions for increasing productivity, Slovakia is recommended to:

6. improve the efficiency and quality of the education and training system and its responsiveness to changing skills requirements (GL 13).
7. encourage R&D and innovation and support the transfer of knowledge through FDI (GL 13).

25. Is-Slovenja

Over the last decade, Slovenia has exhibited stable growth; real GDP has grown steadily at 3-5 per cent since 1993. After a recent slow-down, GDP growth is expected to pick up and gradually draw closer to the potential output growth, estimated at around 4 per cent.

Despite a broadly sound economy and commendable achievements in many policy areas, certain weaknesses remain. While having declined steeply in the last two years, relatively high inflation (5.7 per cent in 2003) is still a cause of some concern and has been recognised as a key policy challenge. The government designed an apt policy to lower inflation in a sustainable way, aiming to create conditions for a successful EU accession. It has pursued structural reforms with the objective to facilitate price liberalisation. Currently, administered prices represent 16 per cent of the CPI – the lowest share of all the acceding countries. However, given ineffective competition in the utilities, and insufficient flexibility in both in the financial sector and the labour market a sustainable reduction of inflation still needs to be confirmed.

The restructuring process of the economy has negatively affected the situation on the labour market; employment in manufacturing industry fell markedly over the period 1996-2000. A shift of labour from this sector to the service sector buffered the economic and social distress, while early retirements were used to attenuate a rise in total unemployment. Although the overall picture concerning the labour market in Slovenia is positive, structural unemployment problems persist. The proportion of long-term unemployment is high, in particular amongst older, low-skilled persons. Furthermore, the low employment rate of workers over 55 years of age is a cause of concern, especially with regard to the challenges stemming from an ageing population.

In order to create the necessary job opportunities and facilitate participation in the labour market, leading in turn to a further improved economic performance in the future, continued efforts to promote entrepreneurship, to stimulate the innovative capacity of the business sector and to enforce effective competition in all segments of the economy are required. Policies in Slovenia should aim at achieving a high degree of sustainable convergence. Against this background, Slovenia faces four major challenges:

- Lower inflation in a sustainable way,
- Increase employment rates, especially for older workers,
- Improve conditions for sustained productivity growth,
- Promote the development of effective competition in all segments of the economy, notably in network industries.

Lower inflation in a sustainable way

Although decreasing, inflation remains relatively high. For 2003, the rate of inflation stood at 5.7 per cent, down from 7.5 per cent a year before. The ongoing decline is an encouraging development, although it seems partly attributable to special factors – related to ceilings on administered price rises and indirect taxes as well as frequent adjustments of excise duties on oil. Inflationary pressure continues to be fed by lack of competition in various sectors, inflexible labour markets, and still widespread indexation mechanisms. Furthermore, other important factors contribute to inflation's perseverance; an accommodating monetary policy and a steady, but now slowing, depreciation of the currency, in particular, add to inflation inertia.

In the run-up to EU accession, the government made inflation a policy priority and adopted a co-ordinated anti-inflation policy measures accordingly. A comprehensive price control plan was enforced, regulating the administered price rises and tax changes in a way not to exceed the inflation rate at the end of the year. As regards the objective of proceeding towards a generalised de-indexation of the economy, a step forward was made in 2003 with the official abolition of interest rate indexation (the 'basic interest rate' or TOM) and the social agreement on a new wage adjustment method. A forward-looking indexation has already been introduced for public sector wages, taking effect in July 2004, whereas for the private sector such a policy yet needs to be negotiated. Moreover, the public finance stance needs to be adjusted flexibly. Also, a more swift implementation of structural reforms is necessary for a sustained disinflation and an improved economic performance.

Increase employment rates, especially for older workers

The employment rate in Slovenia – with 63.4 per cent in 2002, close to the EU average – is one of the highest among the acceding countries. Also, the unemployment rate – decreasing steadily since 1998 to have reached 6.0 per cent in 2002 – ranks amongst the lowest in the group. Nevertheless, its long-term component is high at around 60 per cent, principally among older, low-skilled workers over 55 years of age. With other structural imbalances present in the labour market (youth unemployment, unemployment of disabled persons, gender unemployment gap, low educational level of the unemployed, high regional disparities) to increase employment of elderly has been identified as a particular important challenge. In 2002, the unemployment rate for persons aged 55-64 was 3 per cent, while the employment rate stood at 24.5 per cent, a figure very low compared to the EU average of 40.1 per cent. This is a consequence of the low retirement age, which in 2001 averaged only 57 years. The restructuring of the economy has pushed relatively young individuals into retirement (or unemployment). As a result of the pension reform introduced in 2000, the retirement age has already slightly increased. However, the impact of this reform will only gradually be reflected in a higher employment rate for older persons. A large gap between the employment rates for older workers in Slovenia and the EU is expected to persist.

The main orientation of the employment policy is thus to address the problems of unemployment for elderly people and to stimulate active forms of increasing their employability. This is particularly important in view of the growing risks of financial unsustainability resulting from unfavourable demographic developments. The old-age dependency ratio is expected to rise from 20 per cent in 2000 to 38 per cent in 2025 and 66 per cent in 2050. Furthermore, the promotion of work and active working life is the necessary precondition for combating poverty and social exclusion.

Improve conditions for a sustained productivity growth

The level of productivity, while the second highest amongst the new Member States, remains well below the EU-15 average (69.5 per cent in 2003). Labour productivity growth in Slovenia was relatively rapid over the period 1995-1999, with an average annual rise of 4.8 per cent. However, it decelerated thereafter (2 per cent on average in 1999-2002), placing Slovenia amongst the least performing acceding countries in this period of time. Two elements may hamper a more rapid development in productivity:

First, the entrepreneurial activity of the active population remains relatively low, notably because the administrative burdens affecting both business creation and existing businesses are still high. Efforts have already been made to simplify procedures for start-ups. However, the business legislation and administrative environment could be further improved since bureaucratic and lengthy procedures as well as difficulties in buying land for industrial use still persist.

Second, there is a lack of effectiveness of R&D expenditure in terms of transfer of know-how to the business sector, of patenting and of product or process innovation. With R&D expenditures reaching 1.6 per cent of GDP in 2001, Slovenia ranks first amongst the new Member States but still remains below the EU average. Slovenia also ranks first amongst the new Member States in terms of patent applications with the European Patent Office, but its performances in this field (41 per million inhabitants in 2001) are well below the EU average. In addition, the share of researchers employed in the business sector is low as compared to the public sector (one-third and two third respectively) and innovative activity appears to be weak in the high tech sector.

Promote the development of effective competition in all segments of the economy, notably in network industries.

Slovenia has proceeded towards increasing liberalisation in product markets and in network industries, but effective competition needs to be enhanced. In particular, while the Competition Protection Office is mandated with adequate powers to exercise control over restrictive agreements and any abuse of dominant position and mergers, its administrative capacities both in terms of financial and human resources are insufficient to ensure its proper functioning. Moreover, the current legislation does not allow it to set deterrent fines on anti-competitive behaviour.

In recent years, Slovenia has started liberalising its network industries. In telecommunications, legal market opening was introduced in 2001 and an independent regulatory agency was created in 2002. However, effective competition has not yet appeared in fixed telephony for inland calls where the incumbent still holds 100 per cent of market share. The high price of network interconnections together with regulated low price levels for both local and national calls are the main barriers to the entry of new operators in fixed telephony. As regards the energy sector, large electricity customers (66 per cent of electricity consumption in Slovenia) are free to choose their supplier and since 2002 the largest ones are allowed to purchase electricity from abroad. However, the scope of international exchanges is limited to a maximum of 20 per cent of total electricity consumption. In gas, the largest consumers are since 1 January 2003 free to choose their own supplier (accounting for 50 per cent of gas consumption in Slovenia), but in practice they can not switch to another supplier because of long-term contracts up to 2007 with the incumbent.

Country specific recommendations to Slovenia

Meeting the challenges outlined above requires broad structural reforms as they are laid down in the general guidelines (GL) in Part I of the Broad Economic Policy Guidelines.

In order to lower inflation in a sustainable way, Slovenia is recommended to:

1. step-up structural reforms aimed at liberalising administered prices and advance further with de-indexation, in particular of the wage setting mechanism (GL 5).

In order to increase employment rates, especially for older workers, Slovenia is recommended to:

2. review the tax and benefit systems, with a focus on labour market participation of older workers, and reassess the measures promoting active ageing by means of lifelong learning activities, as well as address the imbalance between temporary and permanent work conditions (GL 4, 8).

In order to improve conditions for sustained productivity growth, Slovenia is recommended to:

3. further reduce the time and costs necessary to set up a new company and simplify the administrative procedures affecting businesses (GL 11).

4. promote R&D and innovation in the business sector and improve the quality of the tertiary level education system (GL 13).

In order to promote the development of effective competition in all segments of the economy, notably in network industries Slovenia is recommended to:

5. strengthen the administrative capacity of the Competition Protection Office, ease the entry of new competitors in network industries, and facilitate the purchase of lands for industrial use (GL 9).