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Renewal in Europe

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Editorial

Klaus Regling, Director-General of the Economic and Financial Affairs DG

Dear Reader

Welcome to this third edition of *European Economy News*, the magazine of DG ECFIN. And there is another important welcome in preparation, as you will read in this issue. On 11 July, the ECOFIN Council of Ministers approved Slovenia's entry to the euro area – Slovenia will adopt the euro on 1 January 2007. This event is a landmark because Slovenia will lead the first enlargement of the euro area since 2001. I should emphasise that euro entry is not a race; each of the euro area candidate countries has its own economic particularities and its own convergence path, some longer than others, but euro-area enlargement is now under way and that is a cause for celebration.

You will find in this edition of *European Economy News* also a report on the 2006 Brussels Economic Forum. This annual DG ECFIN conference invites political and economic leaders and experts to talk about topical economic issues. A further article describes the first 'Annual statement on the euro area' produced by DG ECFIN and presented by the Commissioner – this is a review of economic developments in the euro area, the challenges it faces, and the responses needed. In both of these articles, you will come across the words 'reform' and 'change' repeatedly, and there is a good reason for this. Change and reform have been a part of life for Europeans throughout our history – one need only look back to the Industrial Revolution for examples. And today, the speed of globalisation is driving the need, not only for more change, but also for faster change. In response, Europe must undertake reforms, not just to remain competitive, but also to protect the European Social Model and its values of inclusiveness and equity. The important message from speakers at the Brussels Economic Forum and from the Annual Statement is that it is time to act if we are not to be overtaken by events – Europe has a history of embracing change; it is not new for us. Evolution and adaptation have made Europe what it is today and we do not need to fear more change, as Commissioner Almunia made clear in his address to the Forum.

In a final article on 'bird flu,' we give an insight into the research work done at DG ECFIN. It is clear that if an avian influenza pandemic were to materialise, it could be a human tragedy and a cause of much suffering – and European, national and international authorities are acting to reduce the risk of it occurring and to mitigate any eventual effects on people. However, a pandemic would also have economic consequences and DG ECFIN researchers are studying what these might be, and how great an impact they would have on the EU economy. We intend to report other examples of ECFIN research in future editions of the magazine to give our readers an impression of the scope of the work we do in the DG.

Klaus Regling
Director-General
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Editorial information

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What's new from ECFIN

Bigger is better, confirms the Commission

A Commission report evaluating the benefits of the recent enlargement of the EU concludes that the entry of ten new Member States has been a win-win event for all. Rapid growth in the EU-10 is bringing higher standards of living there, while a wealth of new trade and investment opportunities is being grasped by the EU-15. Importantly, says the report, enlargement is proving a force for modernisation throughout the EU by giving impetus to structural reforms just when they are most needed in the face of the growing presence of India and China on the world stage. 'Many of the doomsday scenarios that preceded enlargement have not materialised', said Enlargement Commissioner Olli Rehn, 'and the clear evidence of the economic benefits for all EU Member States should remove any remaining misperceptions.' The report and Communication, prepared by DG ECFIN and entitled 'Enlargement, two years after: an economic success,' can be downloaded from the 'publications' section of the DG ECFIN website.

The spring economic forecasts: growth on the rebound

Economic growth is expected to rebound in 2006 to 2.3% in the EU and to 2.1% in the euro area, up from 1.6% and 1.3% in 2005, according to the latest economic forecasts from DG ECFIN published on 8 May. The main impulse for growth is coming from industrial investment as businesses gear up for expansion. But there are persistent risks, say ECFIN's forecasters, in particular the oil markets where low spare capacity makes them vulnerable to both actual and potential disruptions in supply. Welcoming the revitalised growth, Commissioner Almunia warned that growing at potential is not enough. To reduce unemployment, "Europe must pursue the path of reforms," he said, highlighting corrections to budgetary imbalances and spending on education, innovation and R&D as the only way to bring unemployment down. The latest economic forecasts can be found on DG ECFIN's website.

Fiscal stance: the importance of good posture

In June, DG ECFIN published the annual report on public finances in EMU. As economic growth appears to be taking off, so it is time for the Member States to begin to reduce the budget deficits that arose from past public spending to encourage growth – and adjust their 'fiscal stance' towards lower deficits and budget surpluses, as required by the revised Stability and Growth Pact. This report assesses the budgetary developments in the Member States, looking at sustainability issues, the role of national rules and institutions in fiscal policy, and the ups and downs of economic performance and how to mitigate this cyclical roller coaster through adjusting fiscal policies in economic 'good times'. The report, 'Public Finances in EMU – 2006', can be downloaded from the DG ECFIN website.

Overall classification of risks to long-term public finance sustainability

Risk categorisation	Country
Low	DK, EE, LV, LT, AT, PL, SK, FI, SE
Medium	BE, DE, ES, FR, IE, IT, LU, MT, NL, UK
High	CZ, EL, CY, HU, PT, SI

Source: Commission services

Welcoming Slovenia to the euro area

A welcoming celebration on 11 July marked the ECOFIN Council's confirmation of 1 January 2007 as the date for Slovenia's entry to the euro area. After the press conference announcing the decision, a celebration was held on Rond-point Schuman in the European quarter in Brussels. Organised by DG ECFIN, the event included unveiling a massive poster of the Slovenian 1 euro coin on the Berlaymont building, a huge euro-cake, euro-cocktails and live music. The Commission, the Finnish Presidency and, most importantly, Slovenian officials and representatives, took part and celebrated the first enlargement of the euro area since the introduction of notes and coins. More information on Slovenia's entry to the euro area can be found on the website of the Bank of Slovenia. http://www.bsi.si/en/

'A Maastricht survivor'...

... is how Jean-Claude Juncker described himself as he recalled the signing of the Maastricht Treaty in 1992. "I am the only active politician left from those who signed," he said. The durable Prime Minister of Luxembourg was addressing the conference 'Experience with and preparations for the euro,' held on 10 to 12 May in Linz, Austria and organised with DG ECFIN support. Karl-Heinz Grasser, Austria's Federal Minister of Finance, opened the conference and participants heard ECB President Jean-Claude Trichet and Commissioner Joaquín Almunia among others speak on preparing to adopt the single currency in light of the experience gained since its introduction. The 'Euro Coins Genesis' exhibition on the history of the euro was also launched during the conference and will travel to other Member States in the near future. The presentations at the conference can be downloaded from the website of the Austrian National Bank. http://www.oenb.at/en/welcome_to_the_oenb.jsp

Jean-Claude Juncker speaking in Linz

Princely partnerships

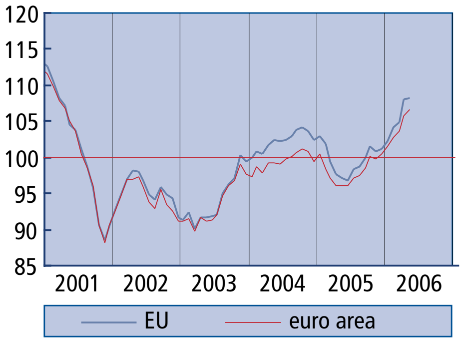
On 5 May the Cypriot Minister of Finance, Michalis Sarris, and the Prime Minister of Malta, Lawrence Gonzi, signed partnership agreements with the European Commission for support in their countries' preparations for adopting the euro. These agreements are part of the 'information programme for the European citizen' (PRINCE) and aim to ensure citizens are adequately informed about the euro in the run-up to adoption. This will be achieved by DG ECFIN support to Cyprus and Malta's communication activities – such as leaflets, media campaigns and conferences for stakeholder groups. Cyprus and Malta intend to join the euro area on 1 January 2008.

Mr Sarris, Mr Almunia and Mr Gonzi

Sentimental economics

DG ECFIN publishes regular business and consumer surveys that report on 'economic sentiment' – the degree of confidence that business managers, high street retailers and consumers, among others, have in the economic outlook. Rising confidence suggests more orders for industry and more action on the high street – both drivers of growth. The surveys published on 31 May report economic sentiment is still rising, continuing a six-month trend. Consumers in particular are more confident about employment prospects; at the country level, Germany and Spain are the most buoyant. The latest business and consumer surveys can be downloaded from the DG ECFIN website.

Economic sentiment indicator (s.a.)
Long-term average = 100



Source: Business and consumer survey results

Euro Team

The upcoming enlargement of the euro area is accompanied by extensive communications campaigns in the EU-10 Member States aimed at preparing their citizens for euro adoption. To support these efforts DG ECFIN is launching the Euro Team Network of expert speakers specialised in euro-related matters. Speaking in the local language, Euro Team experts will present the facts, the challenges and the pitfalls of the euro and the euro changeover process to EU-10 citizens in seminars and meetings, and in their national language.

New skills for the global economy – a workshop

'Adjusting to globalisation: promoting new areas of specialisation' was the title of a workshop organised by DG ECFIN on 12 June. The countries' experiences discussed at this workshop have shown that different strategies may be adopted to adjust to globalisation. For example, while the US has tended to shift specialisation towards new sectors, Germany has built on increasing its comparative advantage in medium-tech industries. However, to be successful the strategies put in place must include some common features, such as increased flexibility, additional efforts in innovation and product differentiation and the reorganisation of production chains, and policy-making can support such adjustments. Workshop participants heard from European and US experts on how policy-makers can ensure that the right economic framework is in place to assist the reallocation of resources into areas of comparative advantage for Europe. Particular experiences in policy implementation from Germany, the US, the new Member States and Ireland were presented.

Covering the euro

In July, journalists from the new Member States attended the first of a series of seminars aimed at acquainting them with the details of EMU and the euro. Organised by DG ECFIN and the European Journalism Centre, the three-day seminars take place in Brussels or Frankfurt, where journalists are introduced to in-depth information on euro practicalities and experiences, particularly in the light of future enlargement of the euro area. As well as presentations from DG ECFIN staff, the journalists also have the opportunity to interview Commissioner Almunia in Brussels or meet ECB President Jean-Claude Trichet in Frankfurt. Further, to ensure no one goes home empty-handed, seminars are timed to coincide with relevant press conferences covering EU economic issues. The July seminar, in Brussels, coincided with the ECOFIN decision to admit Slovenia to the euro area. While mainly aimed at journalists from the new Member States, seminars for third-country and 'old-Europe' journalists are also planned.

Further information

The latest news and press releases from DG ECFIN are available at:
http://ec.europa.eu/economy_finance/news_en.htm

Looking ahead

In the autumn:

The Commission will publish the regular **Convergence Report** for the Member States that are not in the euro area but have committed to join. Produced every two years, the report details the progress these countries have made towards meeting the economic and legal criteria for entry to the euro area.

In September:

The Commission will participate in the **ASEM 6** meeting to be held in Helsinki on 10-11 September, hosted by the EU Presidency. The Asia-Europe Meeting (ASEM) is a forum for political, economic and cultural co-operation between the EU and Asian countries. Globalisation and competitiveness are among the main priorities of this sixth summit meeting, and regional economic relations and development trade negotiations are agenda topics.

In September:

The Commission will attend the **autumn summit** meeting of the IMF and the World Bank in Singapore. Ahead of the summit, Commissioner Almunia will participate in the G7 Finance Ministers meeting on 17 and 18 September in Singapore that will discuss development issues and combating the financing of terrorism. He will also participate in the International Monetary and Financial Committee preparatory meeting on 19 and 20 September, also in Singapore, which will involve an exchange of views on the global economy and financial markets.

In September:

DG ECFIN will publish the **interim economic forecasts** for the EU and the euro area on 6 September. These newly instituted forecasts complement the extensive spring and autumn economic forecasts and provide up-to-date information on the outlook for major macroeconomic indicators.

In November:

On 6 November DG ECFIN will publish the **autumn economic forecasts** covering the EU and the euro area and each Member State individually. These extensive economic forecasts consolidate information provided by the Member States and survey data from Eurostat and DG ECFIN. Published twice a year, the forecasts provide the economic context for policy-making by the EU institutions.

A European round-up

Michelangelo: mint editions

Jean-Claude Juncker and Joaquín Almunia

The 50th anniversary of the Treaty of Rome will be celebrated on 25 March 2007. To commemorate the occasion the euro area Member States will issue a two-euro coin with a common design. The winning design evokes Michelangelo's paving on the Piazza del Campidoglio in Rome, where the Treaty was signed on 25 March 1957. It was chosen by a jury consisting of Pervenche Berès, President of the ECON Committee of the European Parliament, Commissioner Almunia (DG ECFIN), and Jean-Claude Juncker, Prime Minister of Luxembourg and President of the Eurogroup. For more information see 'euro related' in the publications section of the DG ECFIN website. http://ec.europa.eu/economy_finance/publications_en.htm

ECOFIN: a one-stop shop

The ECOFIN Council of Ministers in June considered tax matters, in particular value added tax (VAT) and who collects it in cross-border transactions. This issue is becoming increasingly significant as the number of e-commerce transactions rises, between businesses and from businesses to consumers across the EU. The proposal from the Commission is to change the place of taxation for value added tax for services from the supplier's country to the customer's country. The proposals also include establishing a one-stop shop to simplify the paperwork for companies that do businesses in Member States where they have no base. The Council aims to reach agreement on this issue by the end of 2006. Conclusions of the ECOFIN Council can be found on the website of the Austrian Presidency. http://www.eu2006.at/de/

Balancing globalisation

This was the title of the OECD Forum held on 22 and 23 May in Paris. Participants heard from ECB President Jean-Claude Trichet and others on topical matters such as solving global economic imbalances, managing pandemics and natural disasters, and integrating China into the world economy. Sustainability of pensions and revitalising growth in Europe were among the 'hot' economic issues discussed. 'The direction of economic policy is often portrayed as a straight choice between the US market model and the continental European approach, or roughly stated, between the market and the state,' said John Monks of the European Trade Union Confederation. 'But the success of the Nordic economies in combining high taxes and generous welfare systems with solid growth, strong public finances and moderate unemployment suggests that the problem is more complex.' Further information can be found on the OECD website. http://www.oecd.org/

'Precious time is being lost' ...

...was the comment of Raghuram Rajan, International Monetary Fund Research Director, at the press conference to launch the IMF's annual *World Economic Outlook: Globalisation and Inflation*'. While economic growth forecasts are revised upwards, the Outlook highlights downside risks, such as inflation and higher oil prices. Rajan's greatest concern is a growing 'implementation deficit' in reforms needed for a more competitive, integrated world economy. He also stated that the tremendous pace of private sector globalisation has prompted a public sector backlash with governments pandering to vociferous interest groups rather than educating their citizens on the need for change. Such beggar-thy-neighbour policies should be roundly condemned he insisted, saying, "Economic patriotism is protectionist old wine in a mislabelled new bottle and is all the more dangerous in this interconnected world". The World Economic Outlook can be downloaded from the website of the IMF. http://www.imf.org/external/pubs/ft/weo/2006/01/index.htm

Slovenia: leading the second wave

Europe's finance ministers have approved Slovenia's entry into the euro area – giving 1 January 2007 as the date for adopting the single currency. Convergence reports, published earlier this year by the European Commission and the ECB, had confirmed the sustainability of Slovenia's economic convergence with the euro area, leading to a positive Commission assessment that was discussed by EU leaders at the June European Council. Slovenia will be first of the 'second wave' new Member States to adopt the euro. In the run-up to January 2007, "Slovenia must also now speed up and finalise the crucial practical preparations to ensure a smooth changeover, including measures to avoid unjustified price increases," said Economic and Monetary Affairs Commissioner Joaquín Almunia. The Commission's convergence report on Slovenia can be downloaded from the website of DG ECFIN.

The facts – from the OECD

The 2006 OECD factbook is available on-line. It uses over 100 indicators to give an overview of worldwide economic, environmental and social trends in full colour. If you want to know about Australian crime rates, the idleness of Finnish teenagers, or Korean car accident rates, then this is the factbook to have. Special topics in the 2006 edition include brain-drain statistics, tsunami aid and cultural and leisure activities. The on-line version is free of charge and can be found on the OECD website. http://www.oecd.org/

MEPs concerned

In May, the European Parliament adopted a resolution on public finances in EMU based on a report prepared by MEP Dariusz Rosati of the Committee on Economic and Monetary Affairs (ECON). MEPs expressed concern about persistently low growth in the EU which, the report says, is restrained by structural rigidities, weak demand and an unbalanced macroeconomic policy mix. In the face of a lack of policy coordination in the euro area, shown by the divergence of fiscal policies, the resolution called for the President of the Eurogroup to propose a detailed plan for the duration of his term in office, with regular reports on the level of implementation achieved. The ECON report can be found under 'adopted reports' on the ECON website. http://www.europarl.europa.eu/committees/econ_home_en.htm

G8 Finance Ministers: romantic and mysterious...

...is how the guidebook describes the Mikhailovsky Castle in Saint-Petersburg where the Commission and the EU Presidency joined finance ministers from the G8 on 9-10 June to prepare the economic aspects of the 15-17 July Summit hosted by Russia. The world economy and energy were high on the agenda. Commissioner Joaquín Almunia spoke on energy and development, in particular on the fight against energy poverty in developing countries and the need for carefully designed energy strategies. As well as avian influenza and the fight against money laundering and terrorism, the financial literacy of households was also discussed. This is an issue of rising concern as the responsibility for pension provision falls increasingly on households themselves. The G8 Finance Ministers also met their counterparts from selected emerging market countries and Australia for informal and candid discussions on new donors of development assistance and good fiscal governance.

The euro-area economy: a statement with intent

The first 'Annual Statement on the euro area' takes stock of the euro-area economy at a time when economic recovery is taking hold and 'good times' seem to be on the horizon. As the economic situation evolves, so too must economic policies. In the macroeconomic sphere, the priority is to seize the opportunity created by the improved economic outlook to lock in sound monetary and fiscal policies. In the microeconomic sphere, the euro-area's disappointing record of delivering growth and jobs calls for structural reforms to be stepped up. The main messages of the Annual Statement are summarised here.

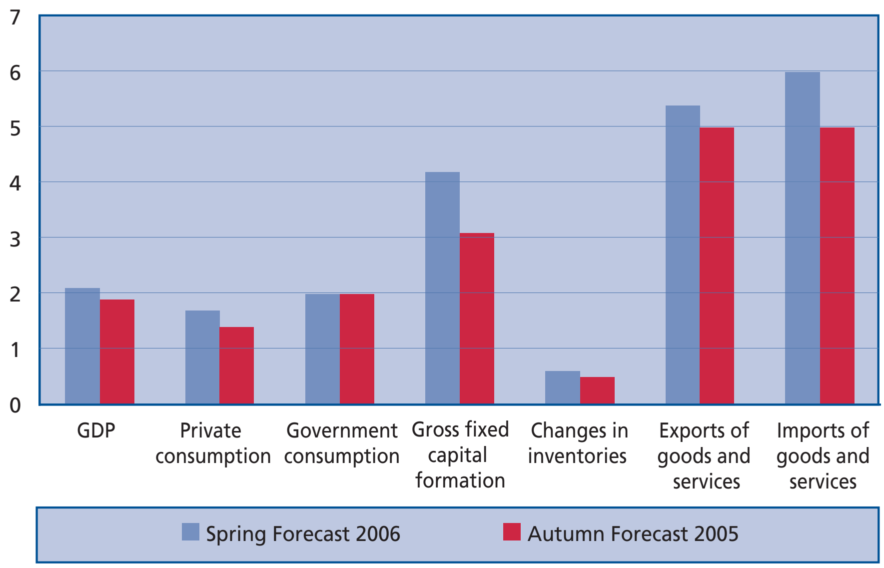
Spring in the air

The euro area is experiencing a sustained recovery in economic activity after several years of below par growth. Regular business and consumer surveys have tracked the growing confidence of industry and consumers in the economic outlook, and this is now translating into growth. Businesses in particular are showing greater optimism – in fact, industry confidence is at its highest for five years. Consumers too are slowly becoming more optimistic, with consumer spending expected to pick up – in line with growth in employment. These positive elements are recognised in the latest economic forecasts prepared by DG ECFIN, which predict GDP growth of 2.1% in 2006 (Chart 1).

Continued expansion of world trade, the strong performance of trading partners, and a pick-up in domestic demand are supporting factors for this more positive outlook. However, there are downside risks – such as further oil price rises – that could stall the recovery.

The twelve euro-area members face a set of shared economic challenges, and while a collective pat on the back may be in order, rising economic growth should be seen as an opportunity to go forward rather than a chance to relax. The euro area must not rest on its laurels but protect what it has won by adjusting macroeconomic policies to promote long-term sustainability, and go further with structural reforms to boost productivity, raise potential growth and create more jobs.

Chart 1: A brighter economic outlook: GDP and its components in 2006



Source: Commission services

Protecting the gains

Monetary policy in the euro area has spurred economic confidence through historically low interest rates. National fiscal policies – taxing and spending – have also supported growth. However, in a time of rising growth, euro-area governments have a responsibility to 'recharge the economic batteries' by doing more to reduce deficits and debts. The revised Stability and Growth Pact (SGP), which provides a blueprint for fiscal discipline in the euro area, specifically calls for efforts to secure budgetary stability to be stepped up when economic conditions are more favourable. In view of the more favourable economic outlook, now is the time to make an extra effort. Failing to take corrective action at this juncture could be very costly in that it would postpone budgetary adjustment until economic conditions are less favourable and reforms are harder to implement.

Room for manoeuvre, room for reform

While appealing for macroeconomic prudence, there is less caution in calling for action on unemployment, as the Annual Statement reiterates the need for economic policies to improve the functioning of EMU and promote higher growth and more jobs. Moreover, the challenges of an ageing population must be met and the opportunities offered by technological advances and globalisation should be seized to create opportunities for all Europeans. The single currency is not to blame for past low growth and unemployment – the real cause lies in the insufficient progress in reforming product, labour and capital markets.

EU leaders have recognised that economic reforms are needed as properly functioning markets play an important role in cushioning the impact of economic shocks. They now need to match words with deeds by stepping up the pace of implementation for the structural reforms envisaged in the Integrated Guidelines.

Dispelling the myths

The Annual Statement makes a point of addressing some 'persistent myths'. 'Economic reform,' it explains, 'is not about giving up a standard of living that Europeans can no longer afford'. Evidence

'... the twelve euro-area members face a set of shared economic challenges'

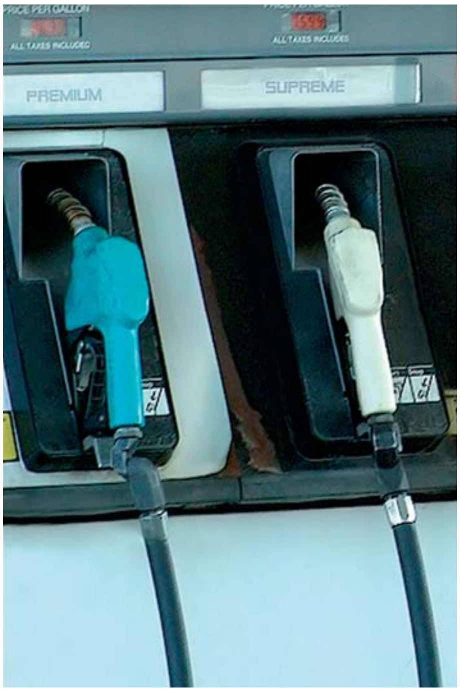
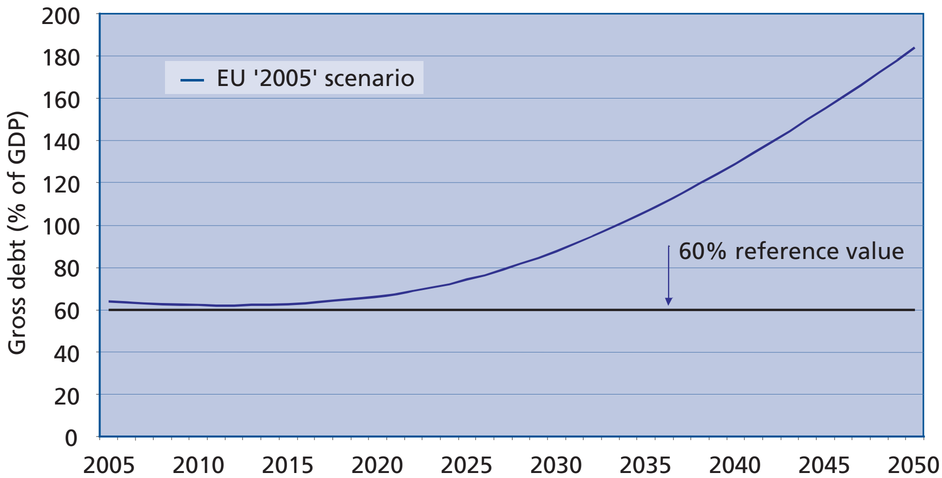


Chart 2: The burden of ageing if nothing is done: EU25 gross debt (% of GDP)



Source: Commission services

presented in a recent study suggests comprehensive reforms of product, labour and capital markets could increase potential growth from 2% to 3% – bringing more jobs, and higher disposable incomes. Fears that reform mixed with globalisation will make Europe 'less European' also receive short shrift. Economic reform, it argues, is consistent with the Treaty of Rome's commitment to economic openness and greater competition.

Policies for all Europeans

Completing the single market is vital if the 300 million people who live in the euro area are to reap the full benefits of the single currency. Fragmented retail markets must be opened up to give consumers a wider choice of savings plans, insurance policies and pension plans. A European response is also necessary to safeguard the sustainability of energy supplies. While calling for solidarity and action to complete the single market, the Annual Statement warns of the dangers of 'economic patriotism,' and calls for today's generation of Europeans to choose economic policies to sustain the Internal Market and foster tangible economic benefits for all.

A strong single currency, a strong single voice

The Annual Statement also considers the global economy and the euro area's growing influence. 'The euro has led to a seismic shift in international financial markets', it says, citing evidence of the widespread and growing use of the euro for international debt, foreign exchange transactions, trade and currency reserves. Such seismic shifts bring influence, responsibilities and opportunities. Global economic imbalances, caused by the record US current account deficit, are a major concern and the euro area can contribute to global economic stability by showing leadership in the international arena. However, leadership requires common positions among euro-area authorities, a scarce commodity at present. Better coordination is needed, for example through a unified representation for the euro area in the International Monetary Fund. This commitment to global leadership would help project the euro area's voice on the world economic stage for the benefit of both global economic stability and the euro area. ■

Discussing common challenges more widely

"After seven years, there is a growing sense of the euro area as a single economic entity whose members are facing shared challenges that require common solutions," explains Joost Kuhlmann, Head of Unit for the Economy of the Euro Area and EMU at DG ECFIN. "For this reason we need a real debate on the euro-area economic priorities among a broad range of actors. To this end, the Annual Statement, and the technical report which accompanies it, was written in light accessible style. The Annual Statement was presented by Commissioner Almunia to the European Parliament on 12 July – the same day as its adoption by the College of Commissioners".

Further information

DG ECFIN website:
http://ec.europa.eu/economy_finance/index_en.htm

The Brussels Economic Forum: Renewal in Europe

The annual Brussels Economic Forum brings together politicians, economists, academics and civil society to discuss timely and important issues facing the European Union, with an emphasis, naturally, on the economics. The 2006 Forum was held on 18 and 19 May against a background of accelerating economic growth, both in Europe and globally. Over four sessions, participants heard from distinguished speakers on the risks that must be managed and the opportunities that must be grasped, and how the message of renewal must be clearly communicated to the people of Europe.


Malcolm D. Knight and Gang Fan


Mario M

The economic outlook: weighing the risks

The main risk to world economic growth today is 'global imbalances,' meaning the record US current account deficit that is financed by high savings elsewhere, particularly in Asia and more particularly in China. While the cause and effects of this 'imbalance' are contentious, the risks are not. A disorderly rebalancing of these deficits and surpluses could stall world economic growth. "So we start with the easy part – weighing the risks," was the ironic opening comment of **Christine Ockrent**, French television journalist and Chair of the first session.

Dr **Gang Fan**, Director of the Chinese National Economic Research Institute, highlighted the complexity of the imbalances and how the opening of the Chinese economy may have played some role, although not enough to explain the US deficit. He also shared ideas on the wider issue of a global currency asymmetry arising from the preponderance of the US dollar as an international currency – a factor that allows the US to spread risk more than other countries. The sustainability of the imbalances was analysed by **Malcolm D. Knight** of the Bank for International Settlements who identified the reluctance to revalue Asian currencies, the amazingly high savings in that region, and low long-term interest rates worldwide that fuel consumption, as reasons for their persistence. As a solution he proposed 'homework' for policy-makers, including: improving the US fiscal deficit, dampening US consumption, strengthening euro-area growth and, given that Chinese savings will remain high because of low social benefits, possibly making policies to make Chinese investment more efficient.

Mario Monti, former European Commissioner, laid out the internal risks to growth in the EU, and in particular in the euro area. Highlighting the divergence of economic performance among EU Member States, he dismissed the offered excuses of differing tax regimes and in-or-out of the euro area as causes – pointing out that these show no correlation with growth performance. Rather, he claimed, the issue comes down to reform and the single market – or the lack of these. "The euro area has less single market than some outside," he claimed, "and it seems to want even less, particularly the larger members who have diluted the single market energy and services directives – this reluctance at the core is a cultural problem, he said, reflecting growing unease in these countries. He called for France, Germany and Italy to reacquire ownership of the market economy that they, as founding members of the Union, created in the first place.

Secretary-General designate of the OECD, **Angel Gurría**, continued this theme of the need for reform. While growth is looking more sustainable, he said, the income gap with the US is widening, not closing. Measures to encourage competition, productivity and innovation are needed. The choice of a particular social model is less important than whether it actually works by contributing to higher growth. "Reform is difficult," he admitted. "The costs are upfront and the losers are vocal." And suggested reforms are presented as win-win packages to gain acceptance. Professor **Daniel Cohen** of the Council of Economic Analysis of the French Prime Minister said that the 1.5% growth gap between Europe and the US is explained by demographics, low implementation of ICT, and 'residual reasons'. Among the latter he contrasted the more effective concentration of R&D into a few universities in the US and the fragmented distribution in the EU. This, he said, needs a pragmatic response involving EU-funded universities.

"Growth is compatible with welfare – but a commitment to reform is vital"

Brigitte Ederer


onti


Angel Gurría


Brigitte Ederer


Poul N. Rasmussen


Susanne Ackum-Agell


Pervenche Berès


Javier Solana


Carl Bildt

Competition and innovation: making it happen

Chaired by Mario Monti, the second session considered the complex matter of encouraging the innovative activities needed to raise growth and productivity and thus raise living standards. **Ian Davis**, Managing Director of McKinsey & Company, kicked off by answering the question 'What should be the drivers of innovation?'. There is much hope invested in innovation as a driver of growth he said, so the issue is how to turn these hopes into reality. For Davis this lies in the link between competitiveness and innovation, in which the former drives the latter to produce productivity-driven growth. Competitive intensity is the main driver of this process, he told the audience. And to really impact productivity, innovations must be done 'at scale,' he said, citing Wal-Mart's IT supply chain investments which, although innovative, only really influenced national productivity figures when retail sector competitors took up the same technologies to remain competitive. His key message is that take-up of innovation is driven by competitive pressure and policies must allow innovation at scale.

Professor **Philippe Aghion** of Harvard University dispelled some myths about innovation in his presentation, such as that it is a homogeneous activity (it is not, he said) or that macroeconomic policy has little role to play (it does, he explained), and argued overall for more targeted policies rather than spreading resources thinly. **Donald Kalff**, former KLM board member and biotech entrepreneur, made the case for the important role large companies should play in the innovation process. They should be acting as a resource for innovative smaller companies, through partnerships, funding or takeovers, which would bring their particular advantages of scale, experience and management to the innovation process. **Rachel Griffith**, Deputy Director of the Institute for Fiscal Studies in London, reported research into the substantial R&D spending of EU companies outside the EU and argued that it is not always effective to target policy at encouraging relocation to Europe.

Social models: fostering faster growth

"Reform means change, and change raises questions and concerns among EU citizens," said **Alexander Italianer**, Deputy Secretary-General of the European Commission in his opening address to the third session. So, when communicating with EU citizens it is important to get across that change is not an end in itself. It has a purpose, which is to fuel and fund EU social systems, he emphasised. Chairing the session, **Brigitte Ederer**, former Austrian State Secretary, noted that the EU is not a uniform bloc and contains several social models that show us that growth is compatible with welfare – but that a commitment to reform is vital. Critically, Ms Ederer concluded, win-win reforms that balance rights and obligations must be sought.

Poul N. Rasmussen, MEP and former Prime Minister of Denmark, spoke on the successful introduction of reforms in Denmark in the 1990s. The important element was the encompassing approach that packaged labour market changes, intelligent public investments and tax reforms together, which were presented as a 'deal' including rights and obligations. While some say that Danish-type reforms can only be implemented in smaller countries, Poul Rasmussen sees no evidence for this. But it is not just a case of transposing the Danish model, he said; rather, the philosophy, the coherence of reform 'packages,' and the inclusiveness – these are the important elements to take over. "Globalisation is bringing a new tempo – permanent and accelerating change which needs a response," he told the audience. "So, for example, people need to feel good about changing jobs several times over their career – not a fantastic message," he admitted, "but we have too few leaders who dare to tell people the truth." The compatibility of high social welfare provision and growth was also highlighted by **Susanne Ackum-Agell**, Director General of the Swedish Ministry of Finance, who also pointed out the correlation between regulated labour markets and openness to trade. In this sense, high social welfare provision can be seen as an insurance for people in an open, globalised economy – part of a 'risk management' approach. Further, to overcome resistance to change, packages of reforms are needed, not a piecemeal approach.

Commenting on the session, **Pervenche Berès**, MEP and Chair of the Economic and Monetary Affairs Committee, questioned whether Nordic-type reforms can be implemented in large countries, suggesting that smaller, more open economies are more accustomed to reforms than inward-looking larger countries. Former President of the Federation of German Industries, Professor **Hans-Olaf Henkel**, supported this contrast, pointing out that there are 25 economies that are in competition with each other, each of which will make its own balance between freedom and equality in choosing an appropriate social model to suit its comparative advantages. The complexity of the situation was also cited by **Andrew Watt** of the European Trade Union Institute who reported that the 'EU no jobs vs US bad jobs' view is becoming more nuanced in recent research as the imperfections of markets and actors are taken into account.

"The magic of enlargement is the political stability that brings economic development"

Javier Solana

Enlargement: will the magic work again?

"I would like to underline two words in the title of this session – 'magic' and 'again'" said **Javier Solana**, Secretary General of the Council of the EU and High Representative for the Common Foreign and Security Policy, in his opening statement. "The magic of enlargement is the political stability that brings economic development. There is no doubt that the reconciliation of Europe has been a great political success, and an economic success that has benefited all," he explained. However, he emphasised that it was crucial to communicate to citizens the scope of recent achievements. Turning to 'again', he warned that it was crucial not to repeat the mistakes of the 1990s by lack of engagement in the West Balkans. "We must be generous to all the Balkans," he said, "and Serbia is central to bring stability to the Balkan region."

Chairing the session, **Carl Bildt**, former Prime Minister of Sweden, spoke on whether South-East Europe is on the road to sustained growth or not, drawing on his experience as High Representative for Bosnia-Herzegovina. Starting in the north, he recalled, "Under communism there was a single weekly ferryboat from Stockholm to Tallinn, now there are 40 departures daily – which gives an idea of the changes. Enlargement has created a zone of peace and stability in the EU-10 with open and dynamic economies, massive trade, exploding productivity and double digit growth." Turning to South-East Europe, "The Balkans, with 100 million people, can offer a similar scenario – although it will involve much more building – so there is a dynamic road ahead." Deputy Governor of the Croatian National Bank, **Boris Vujčić**, offered more detail on the region, citing 5%-6% average growth driven by investments on the upside, but persistent 14%-40% unemployment on the downside. Both **Ali Babacan**, Turkish Minister of State for the Economy and **Klaus Liebscher**, Governor of the Austrian National Bank, highlighted the same point, that the *acquis* is more than a formal requirement – it brings real practical gains.

Closing the final session, **Olli Rehn**, Commissioner for Enlargement, thanked the participants. "We have tested your absorption capacity," he commented. But magic is not the key, he said, rather the right future policies are. Enlargement fatigue is a challenge. "We cannot ignore it, we cannot capitulate, and we must engage with the public in the Member States." **Klaus Regling**, Director-General of DG ECFIN, emphasised that it is reform that will allow Europe to take a leading place in the world economy – and it is time to deliver results on reform. More has been achieved since 1957 than anyone would have believed possible at the time. Our capacities for regional integration are admired worldwide. "Despite the doomsayers, Europe is renewing itself," he claimed, "not enough, not fast enough, but reforms are in process to ensure a prosperous and inclusive society." ■

"Europe need not fear the challenges ahead, they are no bigger than those in the past," Commissioner Joaquín Almunia told an audience of over 1000 participants at the 2006 Brussels Economic Forum. Later, he gave EEN his views on the key issues raised by the participants.

"Growth is ahead, we can see the signs, but renewal needs more than growth in a fast changing world – we have to keep moving and this means change. Both Mario Monti and Angel Gurría made this point forcibly in their speeches, as many others do daily, in the Commission, in the Council, in the Member States. But the time for talking really is at an end, reforms may be difficult and there is resistance – but we cannot stand still. We must evolve and adapt: evolve into a more competitive economy and adapt our social models to support this while preserving European values of solidarity and fairness. For this, the public's trust and support is vital, and the ideas on win-win reform packages raised by Poul Rasmussen are a good way of changing people's mindset. But we are not looking for 'standardisation' in reforming social models, each Member State will evolve and adapt in its own way, as several speakers pointed out. Finally, we must remember that Europe is not just about economics; it is also a political project. Politically, we should be generous with enlargement as Javier Solana said, particularly towards the Western Balkans that have suffered so much, and there are sound economic arguments as well, as we know, that enlargement benefits all Member States. The issues raised in the Forum are pressing and growth is not enough. As I said, the main issue is our willingness to adapt, our willingness to get our act together – and act together."

Predicting the impact of a bird flu pandemic

Last winter, fears grew of a possible avian flu pandemic sweeping the world. In the event, as birds migrated in advance of the summer, the number of cases of sick birds remained small, and as yet there has been no case of human-to-human transfer of the dangerous H5N1 strain of flu. But this autumn, birds will return to their winter habitats – where the infection is concentrated – and fears of pandemic will undoubtedly rise again over the winter. What would be the economic impact of a pandemic, and how much should Europe be preparing for one?

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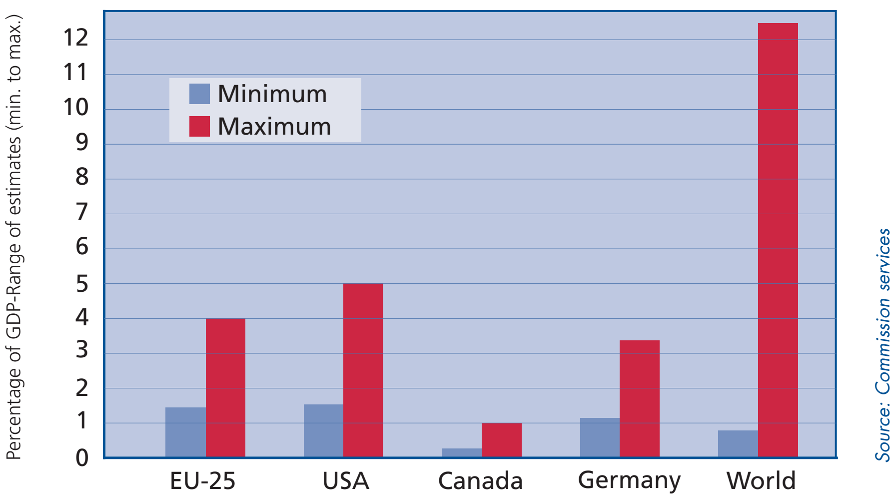
We are as yet several steps away from an avian flu pandemic. Whilst humans working or living in close proximity to diseased poultry have contracted the H5N1 strain of bird flu, as yet there has been no transfer of the disease from human to human. Since few people in the EU have close contact with birds, human-to-human transfer will have to occur before there is a pandemic. Once that takes place, however, features of modern society such as air travel and urbanisation make it likely that the spread of the disease would take place rapidly, although it will not happen overnight.

Whilst we do not know if there will be a pandemic, it is only wise to prepare to deal with the possibility. On the medical front, the pharmaceutical industry aims to develop treatments and vaccines to counter the spread of avian flu between humans (and between birds in the poultry industry), and of course there is the logistical challenge of manufacturing and distributing millions of doses for patients around the world.

In economic terms, such a pandemic would have significant consequences. Millions of people dying and many more ill would inevitably have major impacts on most areas of economic activity. In a recent study(1), Lars Jonung and Werner Röger, senior officials in DG ECFIN's Research Directorate, have attempted to quantify the macroeconomic impacts of a pandemic. They used a DG ECFIN model to assess the effects on the macroeconomic scale for the EU economy. Furthermore, they deliberately used methods which make their results comparable to parallel studies done in the USA, Canada and elsewhere, on the effects of a pandemic.

Jonung and Röger stress that their study aims purely to quantify the impact of a possible pandemic on GDP in the EU, and makes no attempt to factor in the costs of human suffering – which would undoubtedly be significant. They emphasise that the study is undertaken on the same terms as any other attempting to estimate the effects of an external shock on the EU's economy.

Fig.1 Estimated output losses due to a future pandemic – recent estimates



(1) The macro-economic effects of a pandemic in Europe – A model-based assessment', published as European Economy, Economic Papers No 251, June 2006

Past experience

Three influenza pandemics from the past century have been studied by economists, of which the most serious was the Spanish influenza of 1918-19, killing up to 60 million people. Estimates of the economic impact of past pandemics vary however, with some suggesting a negative effect in the long term while others show a positive contribution to growth in their aftermath.

"Whilst we can always find many factors that could influence the rate and extent of spread of the disease, we believe it is reasonable to take evidence from past pandemics as a basis for our assumptions," explains Jonung. Therefore, the study uses the same medical assumptions used in a recent study by the US Congressional Budget Office, which were derived from past pandemics. (This also has the advantage of facilitating comparison between the EU and the US.)

The study assumes a morbidity rate (the percentage of the population infected) of 30% and a mortality rate (the percentage of those infected who die) of 2.5%. On average, those infected would take three weeks off work. That translates to some 150 million Europeans becoming ill, and 3.75 million of those dying (or 7.5 deaths per thousand of the European population). In fact, these assumptions are more severe than the outcome of the Spanish influenza of 1918-19, when the mortality rate was around five deaths per thousand population, and those infected had the fever for just three to five days. Again based on past experience, it is assumed that a pandemic would pass in a relatively short time (within two to three months), and so the immediate effects would be concentrated in a short period.

"Although we have used these assumptions in our model," notes Röger, "the model is scalable and we could easily adapt it to estimate the effects of a different initial impact."

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Supply and demand effects

The study suggests there would be greater effects on the supply side than on the demand side. The study assumes a permanent reduction in the population of 0.75% and an additional temporary reduction in productivity as sections of the labour force take time off while ill, offset to some extent by additional work/overtime by the healthy workforce. Taking supply and demand separately (i.e. ignoring direct influences on each other), the study estimates a reduction of -1.1% in 2006 GDP from the projected level due to supply-side effects and a further reduction of -0.5% from demand-side effects. This total reduction of -1.6% in GDP, were the pandemic to have occurred in the first quarter of 2006, would mean GDP growth would slacken to 0.5%, down from DG ECFIN's projected 2.1% (from the Autumn 2005 Forecast). This reduction in GDP growth falls in the middle ground of predictions for other countries/regions (see figure 1).

Demand-side effects would be strongest in industries such as tourism, travel and entertainment, i.e. non-essential activities that bring people together in large numbers. Member States which rely on tourism for a large share of their GDP, notably the Mediterranean countries, could expect to be hit harder particularly if the pandemic was to happen in the summer months. The model estimates a more limited effect on demand since it assumes the European Central Bank (and other central banks) would lower interest rates to stimulate spending, and the increase in saving during the pandemic would lead into increased spending after it had passed.

Variations

This drop of -1.6% in GDP in 2006 (for a pandemic occurring in first quarter 2006), followed by much less significant drops in 2007 and 2008, would be the equivalent of a major recession. But in contrast to a recession, the economic shock would be concentrated in a short period and the recovery (at macro level) would be much quicker.

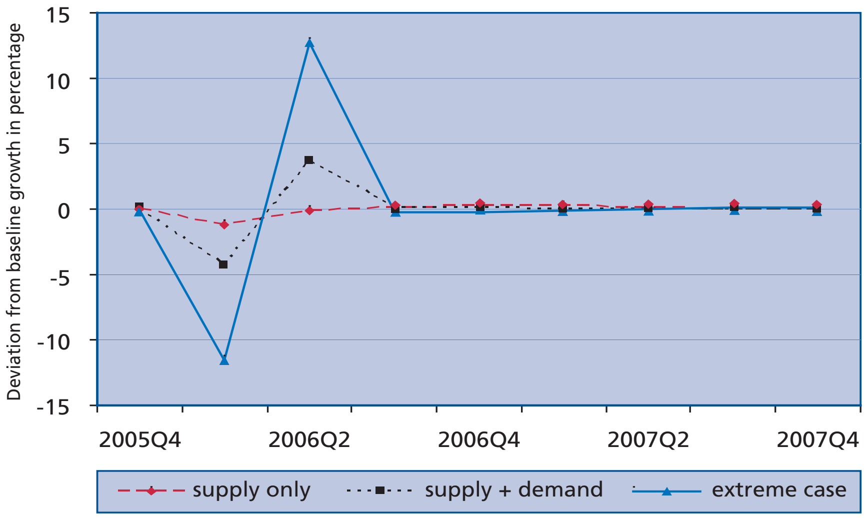
The base assumptions can be varied however, taking account of more severe effects on tourism, or increased disruption to trade due to reduced demand elsewhere in the world. (The impact of the base assumption and a more severe scenario are shown in figure 2.) But one of the biggest assumptions made in the study is that those who are not sick continue to go to work. In the event of widespread absenteeism – whether through employee choice or employer instruction – through a desire to limit exposure to infection, labour productivity would clearly be significantly further reduced temporarily.

"It is difficult to predict rates of absenteeism. We know that in the Hong Kong SARS epidemic in 2003, employers reduced staffing to try and ensure they could maintain key functions running in the event of sickness among their employees," Röger underlines. "Certainly we could see a lot of scope for white-collar tasks to be done by teleworking, so it is likely that more employees could stay home temporarily without disrupting the work flow too much."

Impact

Whilst it predicts the economic effects of an avian flu pandemic would be comparable to those of a recession, the study concludes that there is no major threat to Europe's economic well being, since the effects would be short lived. In contrast to more extreme press reporting on the potential impact of avian flu, this study suggests that the economic effects will be limited. "There is the possibility of being alarmist, particularly since the pandemic may not come, but we have a duty to understand the possible scenarios. Indeed, it's valuable to think ahead, to look at the possible effects on our economy. In fact, given the limited effects we predict, we could even be accused of encouraging complacency," Jonung suggests. "But when we have an estimate such as this study, we can more confidently weigh up the benefits of spending €1 billion on World Health Organisation (WHO) campaigns against avian flu in Asia. Once we have quantified the potential effects for Europe, we see efforts such as that of the WHO in a different light."

Fig.2 Growth effects on EU-25 of a pandemic starting in the first quarter of 2006



Source: Commission services

Further information

The article by Lars Jonung and Werner Röger can be found in the publications section of DG ECFIN's website:

http://ec.europa.eu/economy_finance/publications_en.htm

The economy of Slovenia

© EPA PHOTO / STR

Slovenia (Slovenija)

Currency: tolar

Population: 2 million

GDP per capita in purchasing power standards: €80.9 (2005)
(EU-25=100)

Real GDP growth rate:
3.9% (2005)

Public sector deficit (as % of GDP):
-1.8% (2005)

General government debt (as % of GDP):
29.1% (2005)

Source: Commission services

In the latest in our series of profiles of Member States' economies, we look at Slovenia. Less than three years after joining the EU, Slovenia seems set to be the first of the ten new Member States to adopt the euro. In January 2007, 2 million Slovenes will convert their tolars into euros, but reaching that milestone does not mean that the Slovenian government can sit back. The country still has some way to go to consolidate economic reform, in particular ensuring the economy is less vulnerable to possible shocks.


© EPA PHOTO / ANTONIO BAT

Gaining independence in 1991, Slovenia emerged relatively unscathed from the break-up of Yugoslavia, in contrast to the other new republics that were seriously damaged by conflicts. Slovenia's traditionally strong contacts with neighbouring Austria and Italy, as well as Germany, were a valuable basis on which to build the newly independent nation's economy. Indeed, in comparison with the other new Member States that joined the EU in May 2004, Slovenia's economy was among the strongest.

Despite this strong basis, however, Slovenia has still had to undertake the complex transition to an open, market economy in the years since independence. And once EU membership came into prospect, the goal was to achieve convergence with the euro area. The new Member States have had to undertake significant economic reforms, but Slovenia has travelled most of the transition route without suffering a major shock.

Gradualist

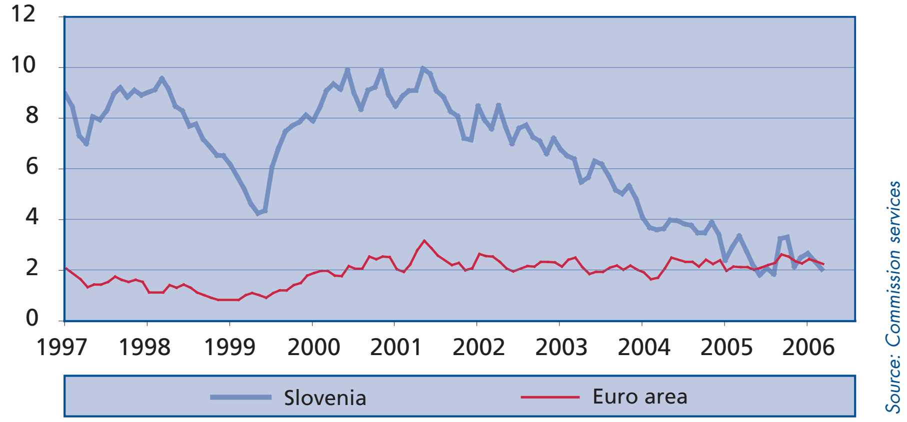
In fact, successive governments' overriding aim in economic policy has been to favour stability, adopting a gradual approach to structural change explicitly designed to avoid major shocks. "This Slovenian 'gradualism' has worked up until now. But that inevitably means there are still considerable challenges facing Slovenia, whereas other new Member States have already dealt with these in response to external shocks which Slovenia has managed to avoid," says Filip Keereman of DG ECFIN. "It will be interesting to observe how Slovenia's economy develops in the coming years, especially once the euro is introduced. Being part of the euro area puts a premium on the Slovenian government advancing with the more painful structural reforms in order to maintain competitiveness and healthy growth."

One success in the Slovenian approach is the stabilisation in the government deficit, reduced from around -4% of GDP in 2000 to less than -2% now. And government debt also is comparatively low, at below 30% of GDP. Following a period of managed depreciation by the central bank, stabilisation of exchange rates has also been successfully achieved in the framework of the exchange rate mechanism (ERM II), which Slovenia joined in June 2004.

Conquering inflation has been the trickiest problem in ensuring the convergence necessary for euro adoption. Around the time of independence in 1992, the inflation rate was in triple digits, but was brought down to about 6% by 1996. The introduction of value added tax (VAT) in 1999, replacing the former sales tax, caused inflation rates to climb to 9% again. Over the past three years, government and the monetary authorities have worked together to control this, and inflation has been reducing steadily

"...the need to enhance the economy's potential has widespread support across the country"

HICP Price inflation (y-o-y percentage change)



since then. In particular, wage agreements in both the public and private sector have ensured there are no excessive rises in consumer spending power, which has limited demand and contributed to lower inflation rates.

Restructuring

In common with other transition economies, Slovenia has seen a shift away from manufacturing towards the service sector. With a 65% employment rate, and a comparatively low unemployment rate of just over 6%, Slovenes have not suffered from industrial restructuring in the way that their counterparts in other transition economies have. However, progress in privatisation has been considerably slower than in most other new Member States.

The private sector accounts for less than two-thirds of GDP, a relatively low share, and the state remains keen on controlling economic actors, either directly or indirectly (through controlling shares in nominally private companies). The public sector still plays a major role in industries such as telecoms, steel, banking and insurance. Part of the problem is a reluctance to cede control of key sectors to foreign investors. Indeed, Slovenia actually has a negative foreign investment (FDI) balance, with Slovenian investments in other former Yugoslav republics in particular exceeding foreign investment inflows.

"Strategic foreign investors haven't been seen as adding strength to the economy, although the current government seems to have loosened policy a bit. There are goals for further privatisation, and some preparation work ongoing, but without much urgency," notes Keereman. "But without attracting external capital, it is difficult to imagine economic growth strengthening to 5%, as the government targets."

In common with all Member States, Slovenia has delivered its national reform programme (NRP) to the Commission, as part of the Lisbon process of fostering growth and creating jobs in the EU. Slovenia's NRP is largely based on the national development strategy. Widely debated, with strong media coverage, the need to enhance the economy's potential has widespread support across the country. And the Prime Minister has recently built on the strategy with a 'partnership for reform' designed to boost the pace of structural changes. This partnership has support from several (but not all) of the opposition parties.

"With the economy seemingly doing reasonably well, it is an opportune moment for further reforms," reckons Keereman. "Tax reform, reductions and restructuring in public spending, and an overhaul of the pension and healthcare systems are all needed to meet the imminent challenges of globalisation and population ageing. To this end, Slovenia also needs to become more business-friendly. There are too many administrative and tax barriers to entrepreneurs and not enough financial support for private enterprise. Moreover, further deregulation and liberalisation is essential to make the economy more flexible, and to enable Slovenia to continue improving its competitiveness."

The euro in Slovenia

The European Commission's recent convergence report, adopted on 16 May, concluded that Slovenia is ready to adopt the euro. The Council confirmed the Commission's corresponding proposal in July; Slovenia will replace the tolar with the euro on 1 January 2007. Under the so-called 'big-bang' scenario, euro notes and coins would be introduced in Slovenia on that day, though there will be a 14-day period of dual circulation when the tolar and the euro will both be legal tender. The success of the big-bang scenario depends on all actors and sectors being fully prepared to switch to the euro immediately as of €-day for both cash and non-cash transactions, in legal instruments, accounting, statistics and for other relevant measures. To help with these preparations, the Commission has concluded a partnership agreement with Slovenia, signed on 8 November 2005, to support its information campaign on the introduction of the euro.

"Slovenia has achieved convergence through a careful implementation of a consistent mix of fiscal, monetary and income policies. The fact that it is the first country of the 2004 enlargement to adopt the euro primarily reflects the strong commitment of the Slovenian authorities to macroeconomic stabilisation and their decisive implementation of the policy objective of euro-area entry," says Massimo Suardi of DG ECFIN.

Further information

http://ec.europa.eu/economy_finance/about/activities/countryeconomy/main_en.htm

Recent research and analysis published by DG ECFIN

2005 pre-accession economic programmes of acceding and candidate countries

EUROPEAN ECONOMY, ENLARGEMENT PAPERS, No. 27, May 2006, European Commission, ISBN 92-79-01383-1.

Pre-accession economic programmes (PEPs) have two objectives: first to outline a medium-term economic policy framework and structural reform priorities that are in line with the requirements for accession; and second, to help develop the institutional and analytical capacities in the accession and candidate countries that are needed for eventual participation in the euro area. In this paper the Commission presents an overview and assessment of the PEPs of Bulgaria and Romania (accession countries), and of Croatia and Turkey (candidate countries).

The legal framework for the enlargement of the euro area

By Torsten Schäfer of DG ECFIN. EUROPEAN ECONOMY, OCCASIONAL PAPERS, No. 23, April 2006, European Commission, ISBN 92-894-8860-3.

In general, recently acceded Member States are committed to adopt the euro and join the euro area after meeting the same convergence criteria as the current euro-area members. However, the way in which the euro is actually introduced in these countries may be different. Some are considering not using a scenario with a transitional period between euro adoption and the introduction of banknotes and coins, while others prefer a 'big bang' scenario in which there is no transition period. This article explains the details and the legal background of the various changeover scenarios and the challenges they present to economic and administrative actors.

Terms-of-trade effects in catching-up countries: the case of the Czech Republic

By Marek Mora of DG ECFIN. COUNTRY FOCUS, Volume III, Issue 4, March 2006, European Commission.

With the lowest GDP growth rate of the EU-10, the Czech Republic's economy might seem to be a 'convergence sluggard' when compared to other RAMS (recently acceded Member States). 'Not so' suggests the author. Terms of trade, the ratio of export prices to import prices, have improved continuously in the Czech Republic from 1996 to 2004, much more so than in other RAMS (except Lithuania). This meant rising incomes for Czech producers, which allowed wage rises above productivity growth, which fed through into increased consumption and rising living standards – so-called 'welfare effects'. So the Czech Republic might be catching up faster than GDP growth figures suggest.

Profitability of venture capital investment in Europe and the United States

By Catarina Dantas Machado Rosa and Kristiina Raade of DG ECFIN. EUROPEAN ECONOMY, ECONOMIC PAPERS, No. 245, March 2006, European Commission, ISBN 92-79-01186-3.

There have been major efforts to encourage the availability of venture capital for European entrepreneurs over the past decade – as part of the Lisbon Strategy for jobs and growth. In this paper the authors sound a warning bell: returns on European venture capital funds are appreciably lower than those in the US, to the extent that they may become increasingly less attractive to institutional investors. However, there is a great dispersion in returns and good performing funds do exist. Further, US returns may be higher because investments were made earlier in the period before the technology bubble burst. Even so, conclude the authors, future levels of investment in European venture capital funds are a cause for concern.

Structural unemployment: a blot on the Finnish success story

By Mart Maiväli of DG ECFIN. COUNTRY FOCUS, Volume III, Issue 5, June 2006, European Commission.

The Nordic countries and the 'Nordic social model' receive much praise as a response to the challenges of globalisation. However, the three EU Nordic countries are not the same. Finland, in particular, has a higher level of unemployment than the others. This arose during a crisis in the 1990s and, despite the spectacular economic recovery and rising employment, persists today. The author ascribes the 'stickiness' of unemployment levels to a lack of an effective 'activation framework' aimed at retraining the unemployed in the skills the economy needs. Denmark is held up as showing 'best practice' in getting people back to work and offers lessons for Finland. While many features of the Finnish labour market are well designed, it is strategically important for Finland to cut unemployment in view of an ageing population, concludes the author.

Mergers & Acquisitions Note

By Directorate E, Economic Evaluation Service, DG ECFIN. No 3, April 2006, European Commission.

Published annually, the Merger & Acquisitions Note analyses M&A activity in the global economy and its consequences for Europe. M&A are an important channel through which firms enter new markets, whether EU companies going abroad or foreign firms setting up in Europe. In addition, M&A activity gets strong media coverage as it can have impacts on employment and security. In this issue, as well as giving an overview of M&A activity in 2005, the authors focus on the EU and China and ask why EU firms have become less attractive for investors, while the opposite is true for Chinese firms.

The Directorate-General for Economic and Financial Affairs publishes frequently on economic research relevant to the European Union; only a selection of these articles is reported here. A complete list of downloadable publications is available at http://ec.europa.eu/economy_finance/publications_en.htm

Selected upcoming publications in 2006:

- Extending work lives: an assessment of reforms to postpone retirement (Special Reports)
- The macroeconomic effects of globalisation for the EU (Economic Papers)
- The Swedish model and the financial revolution (Economic Papers)
- The Scandinavian monetary union: A survey (Economic Papers)
- Financial incentives to postpone retirement (Economic Papers)
- The production function approach to calculating potential growth and output gaps (Economic Papers)

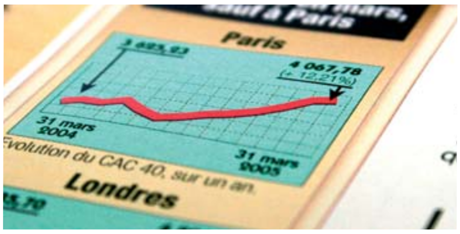
KC-AJ-06-003-EN-C

For your diary

The 2006 ECFIN Research Conference, Brussels, 7 and 8 September 2006

'Adjustment in the euro area: the financial market dimension'

Speakers at the conference include policy-makers, academic economists and financial market experts. They will contribute to exploring ways in which financial markets could give more timely signals to policy-makers and other EMU actors, and will consider the scope for developing institutions that would enhance such 'signalling'. Key issues include: how the economic adjustment process changes, the role of financial markets in the adjustment process, whether converging and steady-state economies face different challenges, what reforms to institutions could improve adjustment in the euro area, and the challenges for supervisory and structural policies. For more information see 'events' on the DG ECFIN website.



Staying in Brussels for... a DG ECFIN workshop on 22 September 2006

on 'Fiscal Indicators in the EU budgetary surveillance'

The workshop will discuss ways to improve the fiscal indicators that are used to measure a country's performance in the light of the broad fiscal rules of the Stability and Growth Pact. Improved indicators are needed to take account of the focus on longer-term objectives and the assessment of cyclical economic conditions in the reformed SGP. The participation and contribution of external experts to such workshops is considered essential to help the technical analyses of DG ECFIN reflect the state-of-the-art of international practice. Participants will include fiscal policy experts drawn from academia, national authorities, international organisations and EU institutions. For more information see 'events' on the DG ECFIN website.

To Berlin for the 7th ECB-CFS Research Network conference on 28 and 29 September

'Financial system modernisation and economic growth'

Organised by the Deutsche Bundesbank, the European Central Bank, and the Frankfurt-based Centre for Financial Studies (CFS), the conference will cover state-of-the-art international research into how improvements in financial systems and related policies can influence behaviour and enhance economic performance and long-term growth prospects – especially in Europe. Keynote speakers include Philippe Aghion of Harvard University and the president of the Deutsche Bundesbank, Axel Weber. For more information see 'events' on the CFS website. http://www.eu-financial-system.org/ecbcfs.html

In Osaka, Japan on 27 October

'A Euro Conference'

A conference on all things euro. Organised by the EU Delegation to Japan in cooperation with Osaka University and the Council of the East Asian Community, this conference is supported by DG ECFIN. It will cover the main developments in the euro area and the opportunities it presents to Japan. For more information see 'events' on the DG ECFIN website.

And on to Spain for the 8th ECB-CFS Research Network conference on 30 November and 1 December

'Financial integration and stability in Europe'

Hosted by the Bank of Spain, this conference will investigate matters of financial integration and stability and how these are related to each other. Other topics include supervisory issues linked to financial integration and the challenges ahead. Keynote speakers include Alexandre Lamfalussy, former president of the European Monetary Institute, the forerunner of the ECB. For more information see 'events' on the CFS website. http://www.eu-financial-system.org/ecbcfs.html

In Nicosia, Cyprus, for a DG ECFIN supported conference on 30 November

'Preparing for EMU and euro adoption'

This is part of a series of conferences on preparations to adopt the single currency in the new Member States. Commissioner Joaquín Almunia, the Minister of Finance of the Republic of Cyprus, Michalis Sarris, and the Governor of the Central Bank of Cyprus, Christodoulos Christodoulou, will speak at the event. For more information see 'events' on the DG ECFIN website.

In Washington DC at the Federal Reserve Board on 1 and 2 December

'The 4th conference of the International Research Forum on Monetary Policy'

This forum encourages research on monetary policy issues that are relevant to policy-making in interdependent economies. Its membership includes the Federal Reserve Board and the ECB. Regular conferences are held alternately in the US and the euro area. For more information see 'news and events' on the website of the Federal Reserve Board. http://www.federalreserve.gov

Further information

A list of the events organised by ECFIN is available at:

http://ec.europa.eu.int/comm/economy_finance/events_en.htm

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