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Making hay while the sun shines

Using growth today, ensuring growth tomorrow

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Editorial

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

Dear Reader

The spring economic forecasts published in May by the Commission give us every reason to be optimistic for the coming years, with their projections of buoyant growth feeding rising employment and confirming the upturn of the economic cycle. And it is also a breath of fresh air for us in DG ECFIN – the opportunity to herald welcome news makes a great change from the more subdued forecasts of recent years. However, while we should all enjoy the good times today and the positive prospects for the next few years, policy-makers should avoid falling into the complacency trap.

The economic good times should not only be treated as a justified reward for past efforts, although we can all take satisfaction from those efforts; they also open a window of opportunity, a resource for the longer term. The opportunity must be grasped and action taken on two fronts. First, we now have the chance to implement much needed structural reforms throughout the Union. The Lisbon Strategy provides a comprehensive and consistent frame for doing so. The Commission has been emphasising the urgent need for reforms in the Member States for some time, as have many others. President Barroso again reiterated the message to delegates to the Brussels Economic Forum this May, saying: "Reform is the name of the game today".

And there is evidence that reforms are starting to take effect, with structural improvements having been made on labour markets. But whether this translates into improvements in labour productivity beyond what can be attributed to the cyclical upturn is less clear. In some individual sectors, such as network industries, it has been shown that reforms have indeed borne fruit in terms of productivity, but these positive results are not yet generalised across the economy. The economic good times we are currently enjoying give us the chance to build on this good start by speeding up the pace of reform to make the European economy fit for the 21st century.

Secondly, there is an urgent need to conclude the long process of fiscal consolidation. Public finances need to be put on a sound footing to provide a springboard for the future. Progress on this front is very encouraging: only one euro-area country is expected to have a deficit of over 3% this year. But it is important that all countries now move decisively to achieve their medium-term objective to ensure that they are well prepared for the next downturn and to face the demographic challenge of ageing. The Eurogroup's statement issued in Berlin on 20 April committing all euro-area countries to use the favourable cyclical conditions to advance rapidly towards their MTOs and to reach them by 2010 at the latest is therefore most welcome.

Klaus Regling
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Editorial information

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What's new from ECFIN

Blue skies ahead for EU economy

The EU economy is set to grow faster than previously expected, according to the Commission's spring economic forecasts. Growth is forecast to hit 2.9% in 2007, despite high oil prices (US$65-70 per barrel in April) and a slowdown in the US economy (expected to drop to 2.2% this year, from 3.3% in 2006). This more vigorous growth rate is partly due to the fact that the economy has performed, on the back of robust domestic demand, better than expected since the last forecast was conducted in the autumn of 2006. This healthy growth is expected to have


A climate for growth

welcome effects in terms of employment and public finances. The EU is on course to create 9 million new jobs for the 2006 to 2008 period, with two-thirds of these in the euro area. The average budget deficit of the EU's 27 Member States is expected to slip to 1.2% of GDP this year, far below the 3% target set by the Maastricht Treaty. The spring forecast can be downloaded from the DG ECFIN website.

EMU: "A European success story"

In a keynote speech at the Athens Economist Conference in April, Commissioner for Economic and Monetary Affairs Joaquín Almunia assessed the successes of EMU and the challenges ahead in the coming years. "EMU has been a European success story," he said. "The positive impact of the euro on macroeconomic stability and economic integration are among [its] many tangible benefits." The Commissioner spoke of five main achievements of EMU and the euro. It has provided economic protection and stability; low and stable inflation rates; and a dramatic fall in interest rates. It has also fuelled European economic integration – boosting intra-euro-area trade by 5-15%, according to conservative estimates. And the euro has also emerged rapidly as the second most important global currency, just behind the dollar. "These achievements notwithstanding, it is clear that the euro and EMU as a whole face challenges," the Commissioner noted. These include disappointing euro-area economic growth, although this is currently being turned around. Read the full speech on the Commissioner's website, accessible from the ECFIN home page.

Slovenia: euro changeover "swift and smooth"

Commissioner Joaquín Almunia described the changeover to the euro in Slovenia in January as "a swift and smooth affair". "This once more underlines the importance of early and careful preparations and of timely information and communication on the euro," he noted. The Commissioner was speaking on the occasion of the publication of a new Commission Communication assessing how successfully the euro was rolled out in Slovenia. Despite consumer fears, preliminary analysis reveals that the impact of the changeover on prices was marginal. Two separate analyses conclude that the overall one-off impact will be in the range of 0.2-0.3%. In fact, inflation in Slovenia has been lower this year than in the comparable period of 2006. A survey of the general public conducted in April 2007 revealed that 83% of Slovenian citizens had no problems adjusting to the new currency and 91% felt well informed. To read the full Communication and the survey, see 'publications' on the DG ECFIN website.

The Brussels Economic Forum

This year's BEF, organised by DG ECFIN on 31 May and 1 June, brought over 1,000 participants together to hear about global imbalances, adjustment dynamics under EMU, and the economic catching-up and convergence process in the EU. President Barroso launched the conference with the headline 'Reform is the name of the game' and the WTO Director General, Pascal Lamy, gave the closing keynote address on the benefits of trade opening. In between, delegates heard a variety of speakers, including Wu Xiaoling, Deputy Governor of the People's Bank of China, on that country's view on solutions to global imbalances, and Marek Belka, Executive Secretary of the UN Commission for Europe and former prime minister of Poland, on the new Member States' approaches to the convergence criteria. Presentations given at the BEF can be downloaded from the 'events' section of the DG ECFIN website.

Time to put the macroeconomic house in order


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The European Commission's 'Annual statement on the euro area' describes the healthiest economic growth for the 13 countries using the single currency since the turn of the millennium. It urges them to use these 'good times' to put the macroeconomic house in order by slashing public deficits and debt. "Policy-makers must strike while the iron is hot, and step up their efforts to put public finances on a sound footing," said Commissioner Joaquín Almunia at the launch of the yearly report. In 2006, economic growth in the euro area was at its most robust since 2000, reaching 2.7% and creating some 2 million new jobs. Healthy growth is also expected this year. However, euro-area governments should not see this as an opportunity to relax. Instead, they must avoid expenditure overruns and use unexpected extra revenues to reduce government deficit and debt. They should also implement further structural reforms, including addressing the issue of wage-price stability. To read the full statement, see 'publications' on the DG ECFIN website.

Measuring euro-familiarity

A new Eurobarometer survey, carried out in March 2007, reports on the degree of familiarity with the euro felt by citizens of the new Member States that are not yet part of the euro area. While many have seen and used the euro, a large number are unclear on the finer design points. Disconcertingly, a majority in all candidate countries think their country can choose whether to adopt the euro or not and do not know that this was a condition of EU accession. However, the number who think this way is slightly less than in 2006. Another worrying figure is that 44% of respondents do not feel well informed about the euro, although this is dependent on how close their country is to euro adoption. Overall, a small majority believe that adopting the euro will have positive consequences for their country, and a larger majority agree it will make them feel more European. The Eurobarometer surveys can be found on the 'euro-related publications' section of the ECFIN website.

Welcoming Cyprus and Malta

A welcoming celebration on 10 July marked the ECOFIN Council's confirmation of 1 January 2008 as the date for Cyprus and Malta's entry into the euro area. After the press conference announcing the decision, a celebration was held on the esplanade of the Commission's Berlaymont building in Brussels. Organised by DG ECFIN, the event included a banner of the Cypriot and Maltese 1-euro coins on the Berlaymont building, a huge book representing a new chapter for the euro area, children carrying flags, euro-cocktails and live music and dancing. The Commission, the Portuguese Presidency, EU finance ministers and, most importantly, Cypriot and Maltese officials and representatives took part and celebrated this second enlargement of the euro area. More information on Cyprus and Malta's entry to the euro area can be found under 'hot issues' on the news section of ECFIN's website as well as on the websites of the Bank of Cyprus and the Bank of Malta. http://www.centralbank.gov.cy and http://www.centralbankmalta.com/

The euro area's "solid expansion"

The European Commission released this year's 2nd issue of its 'Quarterly Report on the Euro Area' on 3 July. The report finds that the solid economic expansion continued in the first quarter of 2007, driven by domestic demand and in particular by

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strong spending on investment. It then goes on to analyse in more depth the recent economic developments in the euro area as well as the short-term prospects. It also assesses the effects of the euro appreciation on household purchasing power and on euro-area exports, revisits the link between fiscal policy and inflation, and presents the mid-term review of budgetary policy in the euro area. Finally, a focus section analyses EU financial integration and its role in euro-area adjustment. The next report for 2007 is due out in October. The QREA can be found under 'publications' on the DG ECFIN website.

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

Looking ahead

In September

The Commission will publish the **interim economic forecasts** for the EU and the euro area on 11 September. The interim forecasts are prepared by DG ECFIN, they appear between the main spring and autumn forecasts, and are based on a more limited data set. They use aggregated macroeconomic data from the larger Member States, in particular on growth and inflation, set in the context of EU-wide economic developments and external factors. The forecast horizon is for the current year, in contrast to the two-year forecasting horizon of the major forecasts. The **autumn forecasts** are scheduled for publication on 9 November.

In October

The Commission will publish a **Communication** on the mid-term review of the Jobs and Growth Initiative. This will establish orientations and promote a convergence of views before the Commission submits its "strategic report" in December (see right). It will lay out why the current integrated guidelines have functioned well and offer a platform for undertaking Lisbon reforms in the Member States, as well as for moving into the next three-year cycle.

In October

The DG ECFIN will publish the next **quarterly report on the euro area**. The QREA contributes to a better understanding of economic developments in the euro area with the aim of informing policy-making and improving public debate on the euro-area economy. As well as presenting a general overview of the euro-area economy, it also contains focus sections that analyse specific, relevant developments and topical issues. This autumn edition will highlight risk sharing in the euro area and the resilience of the euro-area economy.

In November

The Commission will publish a **Communication** based on the *EU Economy 2007 Review* prepared by DG ECFIN. The review is a substantive report on the economic situation and the policy issues in the EU. It is targeted at professionals but is also accessible to non-specialists. As well as forming part of DG ECFIN's economic surveillance activities, the review feeds into the Commission's and DG ECFIN's current work priorities. This year's review will focus on EMU, productivity dynamics and long-term growth.

In December

The Commission will submit a package combining its usual annual progress report on the Lisbon Growth and Jobs Strategy with a "**strategic report**" that assesses the results of the first three-year cycle (2005-2008) of the renewed Lisbon Strategy. Drawing on this assessment, the strategic report will put forward proposals for new orientations for the next period until 2010. It will contain policy proposals for the Community level (revision of the integrated guidelines, a successor to the Community Lisbon programme, follow-up to the actions in the four priority areas) and the national level (country-specific recommendations).

A European round-up

Strengthening the pillars of global finance

In April, DG ECFIN and the US Federal Reserve Bank organised a high-level conference in Washington entitled 'The euro and the dollar: pillars in global finance' which was attended by leading policy-makers from both sides of the Atlantic, including Commissioner Joaquín Almunia. "While the euro has taken its place alongside the dollar as a pillar of global finance, the single European currency is not yet underpinned by a true single European financial market," he told the gathering. Pervenche Berès, chair of the European Parliament's ECON Committee, outlined the main similarities and differences between the EU and the USA and pointed out that regulatory convergence was not just important in the European context, but that it should also occur on a transatlantic basis. For more information see the conference website.
http://www.newyork-conference2007.eu/9.0.html

From open skies towards a transatlantic single market

Integration taking off

The annual EU-US summit, which took place at the White House on 30 April 2007, not only resulted in a groundbreaking 'open skies' deal between the USA and Europe, but the two sides signed a framework agreement to boost transatlantic economic integration. "With the international role of the US economy as powerful as ever and with the EU now firmly back on the growth and jobs path, this is the right time to deepen our economic partnership and to further strengthen the transatlantic economy," said Commission President José Manuel Barroso. "This agreement will allow us to demolish existing, unnecessary barriers posed by divergent regulations and nip new ones in the bud." US President George W. Bush described the agreement as: "recognition that the closer the United States and the EU become, the better off our people become". At first, co-operation will target certain specific sectors, such as the automotive and pharmaceuticals industries.

Pensions homework for all

The Economic and Financial Affairs Council held on 8 May under the German Presidency called on Member States to step up their efforts to raise households' awareness of and participation in non-statutory pension schemes. This was one outcome of the discussion on the financial consequences of an ageing population in Europe. Likewise, the pension services industry should improve the supply of suitable pension schemes while raising standards of advice and customer support. Further, concluded the Council, the Commission should look into whether more work is needed for developing a single market for retirement products. The following ECOFIN Council on 5 June closed the excessive deficit procedures on Germany, Greece and Malta – leaving only seven in force. For more information see the website of the German Presidency. http://www.eu2007.de

Social bridges

Meeting on 20 April, the Eurogroup ministers – from the euro-area Member States – discussed budgetary policies ahead of the start of national budgetary preparations for 2008. This was the first time such a discussion had taken place in the run-up to national budget planning and is seen as a key exercise in fostering fiscal coordination between euro-area Member States. The following day, 21 April, ECOFIN ministers considered how economic and fiscal policies could contribute to building 'social bridges' by supporting employment and social inclusion. A central question was identifying suitable framework conditions so that all citizens have the incentive and capacity to seize the opportunities offered by globalisation and structural changes. The ministers went on to discuss improving the quality of public finances, in particular the effectiveness and efficiency of public spending, which forms close to half of GDP and thus has a marked influence on productivity. For more information, see press release MEMO/07/140 on the Europa press releases page.

Dialogue with ECON

As part of the economic dialogue between the Commission and the European Parliament, Commissioner Joaquín Almunia met the European Parliament's ECON Committee on 7 May to present the Annual Statement and Report on the Euro Area. Exchanges of views with European MPs covered issues such as global imbalances, low productivity growth in the euro area, the balance of the policy mix in view of tightening monetary and fiscal policies, and the potential risks posed by hedge funds to income distribution. On hedge funds, the Commissioner stressed the importance of vigilance by, and dialogue between, supervisory bodies and the need for investor protection. He also noted that the Commission takes a particular interest in income inequalities – which will be the subject of the DG ECFIN research conference on 11 and 12 November this year.

G8 support for Doha

In Potsdam on 18-19 May, G8 Finance Ministers met in preparation for the heads of state G8 summit. Among several items on the agenda, the ministers declared themselves committed to resisting protectionist sentiments and restated support for a successful Doha Round – pointing out that open investment regimes are vital for improving productivity, creating jobs and spurring healthy competition. There were also discussions on hedge funds which, while contributing significantly to the efficiency of the financial system, are now of a complexity that requires vigilance. In this context the ministers welcomed the Financial Stability Forum's updated report on highly leveraged institutions and its recommendations on sound practices and risk management, among others. Ministers also met with finance ministers from African countries to discuss good financial governance in Africa as part of the ongoing efforts to reach the Millennium Development Goals. For more information, see the website of the German federal government. http://www.g-8.de/

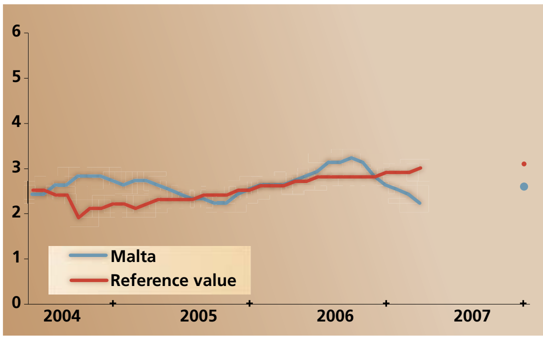

Open trade, fair trade

The euro heads south

The euro-area climate became decidedly sunnier when, on 16 May, the European Commission backed the accession of Cyprus and Malta to the euro area from 1 January 2008. The two islands have not let the surrounding sea hamper their progressive economic convergence towards the other members of the euro area and are now making practical preparations to launch the single currency in the new year.

When Malta and Cyprus joined the European Union in 2004 they committed to adopt the single currency and join the euro area, as did all the Member States that acceded to the Union at that time. However, the timing for adopting the euro was not fixed; rather, it would happen as and when each newly acceded Member State achieved sufficient economic convergence with the euro area. Economic convergence means that a Member State's economy is sufficiently aligned with that of the euro area to ensure that it can participate and prosper within the single currency area.

Figure 1: Malta – inflation criterion since May 2004 *(%, 12-month moving average)*



Sources: Eurostat, Commission services' Spring 2007 Forecast

The rules for economic convergence were established in the run-up to the launch of the single currency in 1999, and all the Member States that joined the new euro area at that time had to meet the same criteria, as laid down in the Maastricht Treaty. For this reason, they are known as the 'Maastricht criteria' or the 'convergence criteria'. They consist of economic, fiscal and legal elements. As well as the compatibility of national legislation, which covers the independence of the central bank in particular, a key requirement is that there is strong evidence that economic convergence is sustainable, and not the result of temporary favourable factors that might not hold in the future. For this reason, when assessing the degree of convergence, particular attention is paid to evidence of price stability, the soundness of public finances, exchange-rate stability and converging long-term interest rates, as shown in the table below.

Presenting their euro credentials

When a candidate Member State considers that its economy is ready for the single currency then it requests an assessment of its economic convergence from the European Commission and the European Central Bank. The governments of Malta and Cyprus did exactly this in February 2007. DG ECFIN analysts performed the assessments and produced positive convergence reports for both Member States. On the basis of these, the European Commission concluded on 16 May that both Malta and Cyprus met the convergence criteria and recommended that they join the euro area in January 2008.

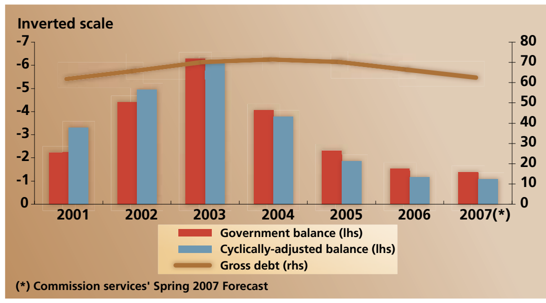
The economies of Malta and Cyprus are comparable in many areas. Both are small, island countries with few natural resources – so that many goods must be imported, as well as energy. Likewise, both are very open, trading economies which quickly achieved a high level of integration into the EU single market on accession. These high imports are counterbalanced by their important service industries; both are strong tourist destinations, for example. However, as small economies they find it difficult to diversify into other sectors and thus remain more susceptible to external shocks.

Malta: on a sound footing

The Maltese economy experienced strong growth in the 1990s as part of its catching-up process, but this went hand in hand with a deterioration of public finances. This was partly due to large government investments in infrastructure, but also to government subsidies to the public sector at the time. At the turn of the century, Malta was hit badly by the worldwide slowdown in the semi-conductor industry and in tourism – both important export sectors for the island. This meant that when Malta joined the EU in 2004 it did so with a government deficit approaching 10% of GDP and debt exceeding 70% of GDP – enough to put the country into the 'excessive deficit procedure', meaning that its macroeconomic performance was not in line with the SGP rules. Since accession, however, Malta has taken steps to fulfil its commitment to join the euro area.

Moderate inflation has been a feature in Malta for some years, the Commission's convergence report points out – with annual averages around 2-3%, although marked by a volatility within each year reflecting the sensitivity of a small, open economy to external events and exchange-rate fluctuations. This can be seen in figure 1 where, despite average inflation staying close to the euro-area average, short-term swings are evident; for example, the peak in 2006 due to higher energy prices. The report finds inflationary pressures have been limited and price stability has been supported by wage discipline and increasing competition in some product markets. Overall, it concludes, price stability is on a sound footing and moderate levels of inflation can be maintained after euro adoption.

Figure 2: Cyprus – government budget balance and debt *(% of GDP)*

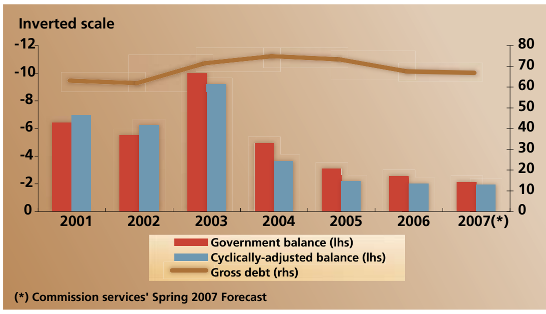


Sources: Eurostat and Commission services

"I believe the economic impact for both Cyprus and Malta should be very positive."

Commissioner Joaquín Almunia

Figure 3: Malta – government budget balance and debt *(% of GDP)*



Sources: Eurostat and Commission services

Improvements are also seen in Malta's government finances with the deficit falling from 10% of GDP in 2003 to 2.6% last year, and the Commission's spring forecasts puts it at 2.1% in 2007 – comfortably below the 3% convergence criterion. Likewise, government debt, after increasing significantly in the approach to accession, has followed a downward path since, to reach 66.5% of GDP in 2006. While this is above the convergence criterion, it is diminishing at a satisfactory pace, notes the report, and thus Malta can be considered as meeting the budgetary criterion. The Commission recommended on 16 May that the Council close the excessive deficit procedure for Malta, which it did on 5 June, thus confirming the country's formal fulfilment of the criterion.

Cyprus: credible policies

Since the mid-1990s, Cyprus has enjoyed steady economic growth of around 4% a year as a modern economy, which owes much to a long period of macroeconomic stability, contained inflation and market-oriented policies. However, on accession there were macroeconomic challenges to be faced: the government deficit topped 6.3% of GDP in 2003 and government debt was around 70% on accession – resulting in Cyprus accompanying Malta into an 'excessive deficit procedure' on EU entry in 2004.

Since accession, a combination of increased tax revenues, structural measures and the containment of public spending have reduced the deficit to 1.5% of GDP in 2006 and a predicted 1.4% in 2007. Over the same period, government debt fell to 65.3% of GDP with a downward trend.

On the price stability criterion the Cypriot economy shares features with Malta, a reflection of both the small size and openness to trade of their economies. So, while volatile to energy and import prices, average Cypriot price inflation stayed close to the EU harmonised consumer price index. This was achieved by supporting exchange-rate stability and a credible monetary policy, notes the Commission's convergence report, helped by a flexible labour market and moderate overall wage increases. In the medium term, says the report, price inflation in Cyprus will depend on energy price developments, as well as on sound fiscal policies and strong wage discipline.

Looking to the future, tourism, business and financial service industries play a major role in Cyprus' external trade, supported by a skilled workforce and excellent infrastructure. However, in manufacturing, with the exception of pharmaceuticals, activities are concentrated in low and medium technology sectors such as foodstuffs, clothing and tobacco. More innovation-driven activities are needed both in manufacturing and services to build the competitiveness of the Cypriot economy as incomes rise to EU levels, to ensure that it flourishes in the single-currency area.

Welcoming enlargement

At the press conference announcing the Commission's recommendation, Commissioner Joaquín Almunia, as he welcomed the coming euro-area enlargement, referred to the particular economies of these two island Member States. "I think the euro provides huge advantages and opportunities to the members of Economic and Monetary Union", he said, "but at the same time I have to say that for economies such as the Maltese and Cyprus economy, the challenges are not always easy and they need to strengthen the work to improve competitiveness and increase resilience." He went on to highlight the need to avoid risks to potential growth resulting from the lack of structural reforms and adequate economic policies that should accompany their integration into the euro area. ■

Further information

More information can be found in the 'hot issues' section on the DG ECFIN website: http://ec.europa.eu/economy_finance/news/hotissues_en.htm

The Maastricht convergence criteria

What is measured	How it is measured	Convergence criteria
Price stability	Harmonised consumer price inflation rate	Not more than 1.5% above the rate of the three best performing Member States; and this level of inflation must be sustainable
Sound and sustainable public finances	Government deficit as % of GDP	Not exceeding the reference value of 3%, unless it "has declined substantially and continuously and reached a level that comes close to the reference value" (Article 104 (2)(a) EC Treaty)
Sound and sustainable public finances	Government debt as % of GDP	Not exceeding the reference value of 60%, unless "the ratio is sufficiently diminishing and approaching the reference value at a satisfactory pace" (Article 104 (2)(b) EC Treaty)
Convergence in long-term interest rates	Long-term interest rates	Not more than 2% above the rate of the three best performing Member States in terms of price stability
Exchange-rate stability	Deviation from a central rate	Participation in the Exchange Rate Mechanism (ERM II) for two years without severe tensions; no devaluation on own initiative

Harvest today's windfalls for tomorrow's shortfalls

Favourable economic conditions over the past couple of years have provided Member States' governments with a precious opportunity to improve the sustainability of their budgets. Whilst those with excessive deficits have done well to bring them down, too little has been done by most Member States to reduce deficits further. The opportunity of good economic conditions should enable all Member States to improve their budgetary frameworks for the longer term, but few are taking real advantage of this. The preventive arm of the Stability and Growth Pact – which has been overshadowed by the deterrent function embodied in the excessive deficit procedure – provides the tools to help Member States improve their budgetary situation for the future, so the Commission is recommending ways to make it more effective.

"If Member States run sound public finances, as a rule, they will never find themselves in a position where they have to correct an excessive deficit," underlined Joaquín Almunia, Commissioner for economic and financial affairs, presenting the 2007 'Public Finances in EMU' report in June. "And that is why the preventive arm of the Stability and Growth Pact (SGP) is of crucial importance."

Whilst he acknowledged the success of Member States in reducing excessive deficits – with all but two expected to bring their deficits below 3% of GDP before the end of 2008 – he expressed a number of worries about deviations from the sound fiscal policy principles of the revised SGP.

"In 2006, the better-than-expected budgetary out-turn was primarily driven by important positive surprises in tax revenues. But part of these revenues were used to finance expenditure that had not been envisaged in the Stability and Convergence Programmes," he noted. "And some Member States are also currently considering tax cuts. However, such measures carry the clear risk of being pro-cyclical and could lead to a worsening of the underlying position of government finances.

"Finally, the budgetary plans of Member States are disappointing. In 2007 and 2008, in spite of a favourable economic outlook, the planned structural adjustment of countries that are not yet at their medium-term budgetary objective (MTO) falls short of the 0.5% of GDP benchmark required by the preventive arm of the SGP," he emphasised. "This means that under unchanged policies, only ten of the 27 EU countries will be at, or will have maintained, the medium-term objective for their public finances, by 2008.

"In the coming years, our main objective will be to ensure a better operation of the preventive arm of the SGP," he concluded. "The aim is to take full advantage of the current economic good times to accelerate the convergence towards sustainable fiscal positions." With that in mind, the Commission welcomes the commitment made, in April, by ministers in the Eurogroup to design 2008 fiscal policy plans "to accelerate adjustment towards the MTO for Member States which have not reached it, and for those which have reached it to avoid feeding macroeconomic imbalances overall".

Learning lessons

"The pattern we have seen in the past couple of years is similar to that which we saw in 1998-2000: economic boom coupled with better than expected tax revenue. And that tax revenue has made a greater than normal contribution to GDP growth," says Elena Flores-Gual, Director in the Commission's Economic and Financial Affairs DG. "On the other hand, too many Member States have shown that they have significant difficulties in controlling expenditure."

The Commission's concern is that many Member States are not taking the opportunity offered by the current economic upturn to put their budgets on to more sustainable foundations. In other words, the efforts they could and should be undertaking now to make the next bust less painful are simply insufficient. In some cases, the windfalls governments have received during the upturn are being spent, rather than used to reduce budget deficits, which would make it easier to accommodate future shortfalls.

It is understandable that governments prefer to focus on short-term benefits, but past economic crises have been deepened because governments have not taken opportunities to make their budgets more sustainable. Longer-term improvements to the fiscal position are essential to ensure sustainability throughout the economic cycle. To reduce the

Medium-term budgetary objectives

First agreed by the Council in 1997, the Stability and Growth Pact (SGP) was revised in 2005, in the light of experiences since the introduction of the euro. A key desire for both the Commission and Council was to make the pact more effective in ensuring Member States' budget deficits do not come close to, never mind exceed, the threshold at which the excessive deficit procedure is triggered (i.e. a deficit of 3% of GDP or more). Whilst the original SGP set each Member State the requirement to keep its budget close to balance or in surplus, the revised pact recognises the need for individual Member States to have greater flexibility to suit their individual economic circumstances, and in particular to support public investment needs.
Each Member State therefore sets its own medium-term budgetary objective (MTO). Effectively, this is the position it aims to reach within the period of its stability and convergence programme, which runs for four years and is revised annually. And the programme sets out the steps it will take over that period to reach the target. For those Member States which have already adopted the euro and those which are members of the exchange rate mechanism (ERM II), the pact limits the MTO to a deficit of no more than 1% of GDP. Moreover, the pact requires those countries to make budgetary corrections each year of 0.5% of GDP in structural terms*, as a benchmark, towards their MTO. Countries outside the euro area or ERM II are not bound by these provisions, but are nonetheless expected to ensure rapid movement towards a sustainable budgetary position.

** Net of cyclical components and one-off measures* chances of excessive deficits in future downturns, the Commission is seeking ways to ensure Member States are more effective in meeting their medium-term objectives now.

Political commitment

"Member States' budgetary plans often leave the ambitious measures until the final years," Flores-Gual emphasises. "And when one year's targets are not met, efforts in the following year are not stepped up, meaning the gap between the target and actual performance increases."

A second problem is that annual government budgets, which are what people focus on, often do not add up to meet the medium-term budget plans. Whilst budgets are usually debated in parliament and given extensive media coverage, in many countries the multiannual budget framework has much less publicity, and may not even be presented in parliament. If it remains a technical document, largely restricted to government use, parliamentarians and the public will not be able to hold government to account if medium-term objectives are not met.

Finding solutions

"In the past, we have seen significant differences in Member States' abilities to meet their medium-term objectives. One factor common to many Member States has been that governments have had difficulties in controlling expenditure," Flores-Gual notes. "In this report, we have analysed what factors have contributed to the success of fiscal consolidation in different countries, and looked at how Member States can stick to their targets better."

The Commission has made proposals in four areas to strengthen the functioning of the preventive arm of the SGP (although it proposes no changes to the rules themselves). These proposals aim to enable all Member States to learn from the successes of others.

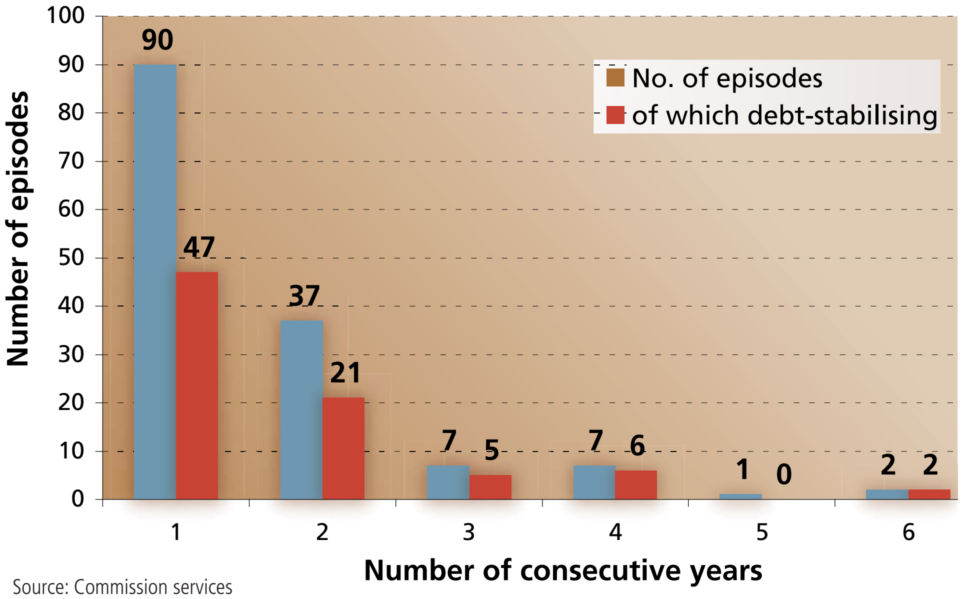
© Emrah Turudu

Broad economic perspective

First, fiscal policy has to be considered more in relation to the broader macroeconomic conditions in the country concerned (and in the euro area as a whole for its members). Factors, such as inflation, external trade balances and competitiveness, need to be understood and factored in when assessing national fiscal policy-making. Moreover, governments need to strive to use public funding more efficiently and effectively, so that demand for services does not lead to ever-increasing expenditure.

The Member States' stability and convergence programmes should therefore place more emphasis on their planned changes to public expenditure and taxation, and the expected effects on the economy. They should also include reforms to budget-making and implementing institutions and procedures conducive to a more efficient use of public spending. Within the euro area, greater emphasis needs to be given to correcting structural imbalances, such as large external trade deficits or surpluses, or inflation, to enable sustainable convergence between Member States.

Figure 1: Frequency of at least 0.5% of GDP improvements of the cyclically-adjusted primary budget balance (CAPB) over consecutive years



Source: Commission services

Member States need to take the opportunity of economic good times to accelerate progress towards sustainable fiscal positions.

National ownership

Second, a major reason for poor performance up to now has been a lack of commitment to budgetary targets from the wealth of public bodies which spend across many Member States. Therefore, national parliaments have to be fully involved in setting the medium-term objectives, as do the different branches and levels of government. Involvement of this nature should enable public bodies to commit themselves to contributing to meeting the targets.

The Commission would also like to see governments going further, to incorporate the provisions of their stability and convergence programmes into national rules, thereby strengthening their political aspirations. In that respect, it has found that those Member States which have created rules-based multiannual financial frameworks have been much better at sticking to budgetary objectives, in particular on the expenditure side.

Reliable and credible targets

Third, past instances of budgetary targets being missed risk diluting confidence in the medium-term objectives, particularly if governments continue to fall short. It is therefore essential, for credibility, to set targets which are achievable, so the growth forecasts, used as the basis for budgetary planning, need to be realistic.

The Commission is also recommending to Member States that they be much more explicit in their stability and convergence programmes, outlining the policy measures needed to meet the targets they have set themselves. Furthermore, the programmes should also set out, in parallel, projections for budgetary variables with no change in policy, showing the gap between the two and, by extension, the size of the task faced by that country.

Medium-term sustainability

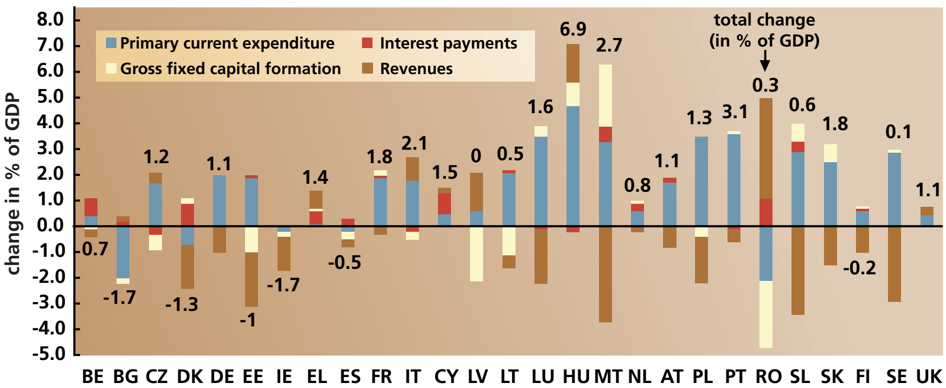
Fourth, Member States' governments face difficult choices over structural reforms and how to achieve fiscal consolidation. Both are essential, so budgetary programmes need to be drawn up realistically to ensure sustainability of public finances. Given past performance, better understanding of the reasons why targets were missed is needed for improving performance in the future.

The Commission intends, in the coming years, to put forward a revised framework for setting medium-term objectives which takes greater account of sustainability of public finances. This will be a valuable tool to achieve budgetary consolidation in the longer term, with revised medium-term objectives for each Member State established to ensure they are better equipped to tackle the challenge of ensuring sustainability in the face of demographic change.

In addition, when it assesses stability and convergence programmes, the Commission will focus more attention on past performance in meeting targets. In the Eurogroup, the Member States which have adopted the euro could go a step further, comparing annual budgets with their medium-term targets, and feeding into the mid-term review of fiscal policies. This review aims to foster coordination of fiscal policies amongst the member countries.

© Erick Nguyen

Figure 2: Composition of the variation in the budget position 2006-2009 (% of GDP)



Note: A positive value indicates a positive contribution to the change in budgetary position. A positive value in total variation of budgetary position (value is presented on top of columns) indicates an improvement in the balance.

Source: Commission services, on the basis of the 2006/07 updates of the Stability and Convergence Programmes

Peer pressure

The Stability and Growth Pact, in its preventive arm, has no sanctions for Member States which do not meet their objectives. Rather, the aim is to use peer pressure to encourage governments to stick to the path towards fiscal consolidation and more sustainable budgets. Whilst, overall, Member States' performances have been disappointing, some have stood out. Indeed, some Member States have set themselves, and achieved, far more ambitious targets than the benchmarks set out in the SGP. The Commission's task in the wake of this report is to encourage other Member States to follow their example and raise their own standards.

Further information

The Public Finance Report can be found at:
http://ec.europa.eu/economy_finance/publications/publicfinance_en.htm

On the road with the euro

DG ECFIN has launched a new travelling exhibition with the aim of communicating the facts, the figures, and the benefits of the single currency to the general public. With many Member States preparing to adopt the euro over the next decade, the push to inform citizens about the single currency is gaining momentum. Of course, most of us know what it is, but do we know why it came about, and how? Surveys from when euro cash was launched in 2002 reveal that in those countries where the general public were well informed, the euro was also well received. So, informing citizens on the euro is a critical part of preparations for entry into the euro area.

Commissioner Joaquín Almunia and DG ECFIN Director-General Klaus Regling.

Entitled 'The euro our currency', the exhibition was launched on 4 June at the Berlaymont building in Brussels. Opening the exhibition, Commissioner Joaquín Almunia explained its mission. "We are paying a lot of attention to communicating about the euro. We need to explain the history, to citizens of both the old and new Member States – about why the decision was taken for a single currency, not only as an economic instrument, but also for political reasons, as part of the process of building our common identity in Europe." He continued, "It is easy for experts to understand, but for ordinary people this unique experience should be explained, as well as the political compromises that are involved. Before, we only had aspirations, now we have good experiences to share: the lower prices, lower interest rates and economic resilience the euro has brought about – its advantages are real and huge."

A walk through the euro area

The exhibition starts by explaining the reasons for a single currency, in particular the search for economic stability and a complement to the single market, and describes the key players and policies during preparations for the single-currency area. It then moves on to describe the many benefits the euro has brought. These include: lower interest rates for borrowers, which spread wealth more; easier trade within the single market, which creates jobs; the integrated financial market, invisible to many, but a real boost to investment in industry; and the resilience to economic shocks, such as higher oil prices, that the euro provides to the economy – a force for stability, just as the founders had hoped.

Unity and diversity

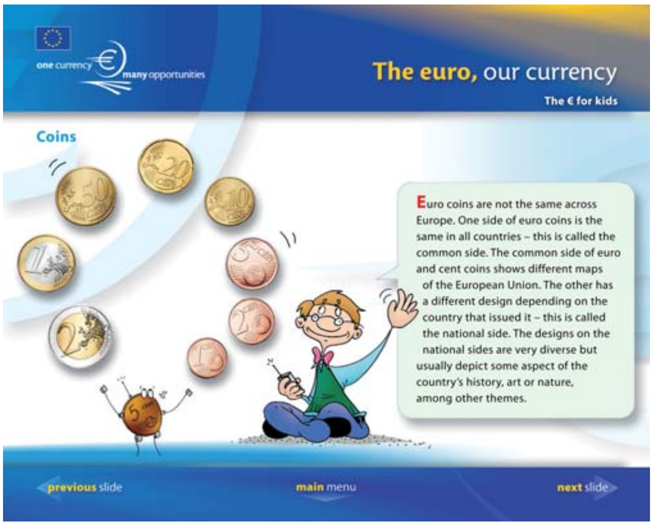
The exhibition is laid out in thematic islands, each dealing with a different aspect of the euro. The section on euro coins gives visitors the chance to see the wide variety of coins in circulation. While euro cash can circulate freely and be used throughout the euro area, few Athenians will come across Finnish coins in their loose change. But here they can see all the different national designs for each denomination and learn about how they were selected, who produces coins, and how many are in circulation. Designs from the Vatican City, San Marino and Monaco are also shown, since these states can issue their own euro coins in amounts set by the European Central Bank. And the designs selected by the countries preparing to join the euro area are presented. The coins of course do not exist yet – but, one day, Vytis the Lithuanian knight and the double cross of the Slovak Republic will be in our pockets and purses. In addition, the rarer 2-euro commemorative coins are presented; every euro-area country is allowed to issue one commemorative coin per year, for example, celebrating World Youth Day in Cologne in 2005 (Germany) and the 2004 Olympic Games (Greece). The next island looks at euro banknotes, their manufacture, distribution and security features. The different representations of the 'Ages and Styles of Europe' which feature on the notes are explained, as is the role of the ECB in decisions on production volumes. Euro banknotes in circulation today would reach to the moon and back 30 times if laid end to end, and all the coins weigh the equivalent of nine cruise ships, visitors are told.

Hot issues

The final thematic island looks at how the euro area is governed, and the current issues and challenges it is facing. The Maastricht criteria, which set out the conditions for entry to the euro area are described, as is the Stability and Growth Pact which guides economic and budgetary policy-making inside the euro area. The importance of sound public finances is also explained in the light of the demographic challenge of an ageing population that will lead to as many people over 60 in Europe as there are under 25 years old in the coming decades.

This section also deals with some of the key messages aimed at citizens in those countries that are preparing

Information on the euro is vital for preparing citizens of countries set to join the euro area.



A slide from the exhibition's touch-screen presentation of the euro for children

to adopt the euro. "Surveys show that citizens in the euro area appreciate the cheaper and easier travel and the ability to make price comparisons that the euro brings", says Stefan Pflüger, Head of DG ECFIN's External Communication Unit, which organised the exhibition, "and they also agree that the euro makes Europe stronger. However, the same surveys also reveal that many perceive that the introduction of the euro brought price rises for consumers despite the fact that statistics show that little overall price inflation occurred when the euro was first introduced." This perception linking the introduction of the euro to price rises has been studied in detail; while consumer perceptions of inflation usually track actual inflation quite closely, following the introduction of euro cash a 'perception gap' opened, whereby inflation was perceived to be higher than it actually was. Studies reveal several reasons for this gap – one being the unusual price rises during the euro-adoption process that were observed, mainly for low-value frequently purchased goods and services such as a cup of coffee, a meal or a haircut. Because these are frequent purchases they weigh more heavily on people's judgement of inflation, even though overall price inflation is hardly affected by the euro.

"This is a key piece of information we want to get across," explains Pflüger. "We know that if people are well informed then these perceptions play a much smaller role in their satisfaction with the euro – forewarned is forearmed as they say. This is shown by the recent experiences from Slovenia."

Lessons from Slovenia

In the same week that the exhibition was launched, a conference in Brussels reviewed the euro-adoption process in Slovenia at the beginning of this year, where surveys reveal that 95% of those polled feel the changeover went smoothly and the information they were given was excellent. Nada Serajnik-Sraka of the Slovenian government communication office detailed the extensive information campaign in the run-up to adoption. Direct communication through helplines, websites, meetings and presentations in schools and shopping centres played a large role, minorities and special needs groups were identified and targeted, and all households received mailings on the euro and dual-pricing. Genovefa Ružić of the Slovenian National Statistical Office reported that more than 80% of Slovenes expected price increases, and some unusual price rises were observed around the time of the changeover for some frequently purchased small items and services, just as when the euro was first launched. However, overall prices moved normally and, in fact, Slovenia experienced price deflation during the changeover period.

Manca Novinec of the Slovene Consumers' Association described the huge public interest in the pricewatch scheme that the association started early in the adoption process. Unusual price rises were identified, investigated and added to a 'blacklist' on the pricewatch website. Public participation was significant, with over 1,800 reports from consumers on price increases. "Slovenian consumers have become more sophisticated and know their rights," she stated.

"The lessons from Slovenia, where the changeover process went very smoothly with much public support, demonstrates the value of a well-planned extensive information campaign," says Pflüger. "As other Member States prepare their citizens for the euro, communication and information will play a major role in ensuring the process goes smoothly and that it is supported by the public. The travelling exhibition will complement national information campaigns and is a part of the effort to raise awareness about the euro and address people's fears by ensuring they are well informed." ■

Further information
Find out more about the subject at:
http://ec.europa.eu/euro

The Commissioner and Director-General learn more about the exhibition from Stefan Pflüger, head of DG ECFIN's External Communication Unit.

The economy of Slovakia

Bratislava – an economy on the up

Slovakia experienced a less painful transition than some of its neighbours from a centrally planned economy to a market economy, without, for example, hyperinflation or high poverty rates. Driven by rapid productivity growth accompanied by low inflation, the Slovak economy today is among the most dynamic of the ten mainly Central and Eastern European countries that joined the EU in May 2004. However, it still lags some of its peers in terms of per capita income levels.

Slovakia has traditionally had a strong focus on heavy industry. Under Communism it was an important centre for heavy machinery, metals and steel production. Building upon these manufacturing traditions, Slovakia's key industries today are automobiles and electronics, both of which have attracted a large number of foreign investors eager to take advantage of a cheap and skilled workforce, favourable tax rates and geographic location and a relatively liberal labour code. Car manufacturers PSA Peugeot Citroën and Kia Motors Corp. both opened new factories last year, and electronics giants Sony Corp. and Samsung Corp. also have operations here. This foreign investment is concentrated almost exclusively in western Slovakia, creating a wide gap with the east. The best-known Slovakian firm is probably the Bratislava-based low-cost carrier SkyEurope.

Late but impressive reforms

Slovakia gained independence on 1 January 1993 following its peaceful 'Velvet Divorce' from Czechoslovakia. Economic reforms slowed in 1994-98, but then regained momentum under a reform-oriented coalition government which laid down important economic and political changes that paved the way for Slovakia to enter the European Union in May 2004. Amongst other things, the government restructured enterprises and banks and initiated large-scale privatisations in a transparent process open to foreign investors. Today, nearly the entire banking sector and many big enterprises are in the hands of foreign owners. Almost immediately after the government had won a second term, it introduced wide-ranging reforms in the tax, pension, social and health care systems, including, for example, a flat income tax, the introduction of a mandatory funded pension pillar and better-targeted social benefits. These reforms increased incentives to work, create jobs and invest, thus fostering growth and economic catching-up.

The coalition government, which came to power following parliamentary elections in June 2006, has pledged to modify some of the economic reforms initiated by the previous government; it has also put a priority on achieving a more equal distribution of income. The government has reiterated Slovakia's commitment to join the euro area by January 2009, in contrast to several other new Member States that have pushed back their timetables amid inflation rates above the entry criteria.

Path to the euro

Upon joining the EU in 2004, Slovakia pledged to eventual entry into the euro area and the adoption of the single currency, joining the exchange rate mechanism, ERM II, in November 2005. An important part of this process concerns the 'convergence programmes', prepared by each Member State and submitted to the Commission and the Council for assessment. These programmes, part of the Stability and Growth Pact, together with the National Reform Programmes submitted under the Lisbon process, outline the economic measures each country will take to ensure healthy public finances, price stability and sound structural conditions for successful participation in the euro area, strong and

Slovakia (Slovensko)

Currency: Slovak koruna

Population: 5.4 million

GDP per capita in purchasing power standards (EU-25=100): >60% (2006)

Real GDP growth rate: 8.3% (2006) (average 5.6% 2002-2006)

Public sector deficit (as % of GDP): 3.4 (2006)

General government debt (as % of GDP): 30.7 (2006)

Inflation: 4.3% (2006)

Current account balance: -7.7% (2006)

Source: *European Commission*

Low inflation rates have enabled Slovakia's government to maintain its target of euro-area entry in 2009.

sustainable growth, and job creation. The currently very good economic times offer a unique window of opportunity to move ahead with fiscal consolidation and further structural reforms.

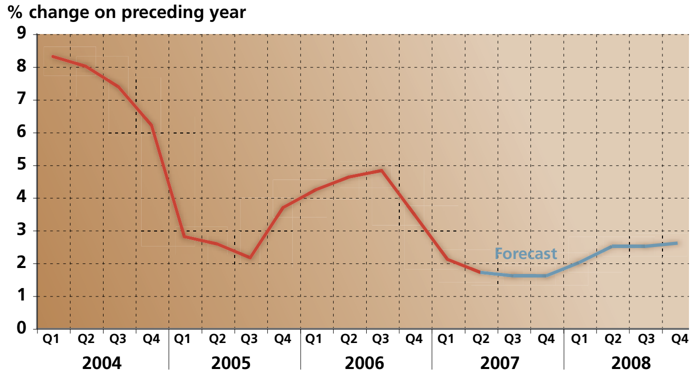
In its updated convergence programme published in November 2006, Slovakia reiterates its goal of adopting the euro in 2009, among other key objectives for 2006-2010. The main fiscal objective is to reduce the general government deficit to under 3% of GDP in a sustainable manner by 2007, thereby meeting the criterion for entry into the euro area. Another goal is to reduce the cyclically adjusted general government deficit adjusted for one-off and temporary effects to below 1% of GDP, in line with the SGP.

On 19 March, the Slovak koruna's central parity rate was appreciated by 8.5% to 35.4424 against the euro, a move approved by the European Central Bank, the finance ministers from the 13 euro-area countries and the finance ministers and central bank governors of the Member States participating in the exchange-rate mechanism. As stated in the official communiqué accompanying the decision, "The re-evaluation should support the authorities in maintaining macroeconomic stability. It is based on a firm commitment by the authorities to pursue appropriate supportive policies, aimed in particular at achieving price stability in a sustainable manner and underpinning external competitiveness and economic resilience. The EU will continue to closely monitor macroeconomic and exchange-rate developments."

Inflation, as measured by the harmonised index of consumer prices (HICP), is expected to fall to 1.7% in 2007 from 4.3% in 2006, according to the Commission's forecasts, as a result of lower increases in regulated prices in the energy sector and a substantial appreciation of the koruna against the euro over a period of several months. Assuming that only moderate adjustments in regulated prices are implemented in 2008 and the exchange rate remains around current levels, average annual inflation is expected to increase to about 2.4% in 2008, according to the Commission services.

Energy prices have had a significant impact on inflation in recent years, with gas and electricity prices in January 2006 among the highest in the new Member States. This can be traced to a tradition of high energy inefficiency going back to communist times and to the lack of competition among energy providers. However, this situation can be improved by promoting higher efficiency and import diversification.

Harmonised index of consumer prices



Slovakia has enjoyed several years of sustained economic growth, boosted in large part by direct foreign investment and manufacturing. The Commission has forecast GDP to rise by about 8.5% in 2007, surpassing last year's record 8.3% growth, fuelled primarily by domestic demand, and then to slow down to about 6.5% growth in 2008. Exports are expected to outpace imports in coming years, leading to a significant reduction in the trade deficit and net foreign borrowing.

Strong domestic demand and newly built export production capacities – such as new car production plants – should give a boost to employment, which increased by 2.3% in 2006, while the unemployment rate dropped by almost 3% to 13.4% of the labour force. This decrease can be attributed in part to many Slovaks moving away to work abroad. However, long-term unemployment is hovering at around 10% of the labour force, due in part to the lack of job opportunities for lower-skilled workers.

The castle in Bratislava

Recent developments in public finances

The government launched a pension reform in 2005 which had the effect of redirecting 9% of gross wages to a second, or funded, pension pillar. As a result of a gradual transition and strong participation in the scheme, these revenue transfers are estimated to have increased from 0.8% of GDP in 2005 to almost 1.2% of GDP in 2006. A January 2006 increase in excise taxes on cigarettes and alcohol spurred many citizens to stockpile these products towards the end of 2005, which had not been foreseen in the 2006 budget and had a negative impact on 2006 tax revenues of around 0.25% of GDP.

Nevertheless, higher than expected GDP and employment growth combined with lower interest expenditure assured that the 2006 government deficit – including pension reform costs – ended up at around 3.4% of GDP. As a result of strong economic activity and restrained public expenditure growth, the government deficit is anticipated to fall below 3% of GDP in 2007 if the government implements the 2007 budget in full.

"Slovakia is making progress with fiscal consolidation, but it appears that the present favourable cyclical conditions are not being fully exploited to reduce the budgetary deficit even further in order to ensure that the correction of the excessive deficit can be maintained even when the current strong growth eventually abates," said Filip Keereman, head of the ECFIN unit responsible for monitoring and analysing Slovak economic and budgetary developments. ■

Further information
More information can be found on the Member States' country pages on the DG ECFIN website:
http://ec.europa.eu/economy_finance/about/activities/countryeconomy/main_en.htm

Recent research and analysis published by DG ECFIN

Growth, risks and governance: The role of the financial sector in southeastern Europe

By Valerie Herzberg (EIB) and Max Watson (Oxford), DG ECFIN. OCCASIONAL PAPERS, No 29, April 2007, European Commission. ISBN 978-92-79-04687-2

The accelerating development of the financial sector in south-eastern Europe could contribute strongly to real economic convergence with the EU. And this is taking place against a backdrop of low inflation and several years of sustained growth. The authors explore the challenges posed by this rapid development and assess opportunities and risks. They then discuss the structural and institutional reforms needed to underpin healthy financial expansion, and consider their interaction with macroeconomic policies in promoting growth and stability. The article concludes by discussing the priorities and trade-offs facing policy-makers.

External imbalances in Croatia – a matter of concern?

By Uwe Stamm and Mihai Macovei, DG ECFIN. COUNTRY FOCUS, Volume IV, Issue 6, May 2007, European Commission.

A special country focus sounds a note of caution over the level of foreign debt clocked up by Croatia. The authors argue that a rise in external indebtedness has made Croatia more vulnerable to potential shocks. However, since that increase has mainly been investment-driven and has not been accompanied by a fall in savings rates, the authors are not unduly worried. In addition, the sizeable foreign assets of the banking system and evidence about the existence of unrecorded foreign exchange holdings by the private non-banking sector can soften any possible blows. The paper concludes that further fiscal consolidation remains a key tool in addressing these external vulnerabilities and facilitating further growth in private-sector activities. In this context, deeper structural reforms could trigger a stronger supply response, raise potential output, and improve competitiveness on a broader front.

Adjustment in EMU: A model-based analysis of country experiences

By Sven Langedijk and Werner Roeger, DG ECFIN. ECONOMIC PAPERS. No 274, March 2007, European Commission.

This analysis sheds light on the debate as to whether the single European currency is having a converging or diverging effect on euro-area countries. One school of thought maintains that the diversity of European economies would be accentuated by the introduction of the euro, while others argue that it would assist economic integration. The authors consider six very different euro-area economies: Germany, Spain, Ireland, Italy, the Netherlands and Portugal. The analysis reveals that growth and inflation developments and current account shifts did occur but that these can largely be attributed to a one-off adjustment which now seems to have run its course. In addition, the absence of an exchange risk premium in EMU has bolstered capital mobility, resulting in a lower correlation between domestic savings and investment.

Provisions of the welfare state: employment protection versus unemployment insurance

By Michael Neugart, Wissenschaftszentrum Berlin für Sozialforschung. EUROPEAN ECONOMY, ECONOMIC PAPERS, No 279, May 2007, European Commission. ISBN 978-92-79-04632-2

Employment protection measures, such as high costs of firing workers, and employment insurance measures, such as unemployment benefits, are the main instruments for workers to protect themselves against the risks of unemployment. Societies generally emphasise either one or the other in their employment legislation – they seek a balance. This article looks at how different countries decide on where the balance should be and shows how supportive family ties play a role. The author then discusses the lessons for policy-making and, in particular, the implications for 'flexicurity', suggesting that governments need to understand the reasons for their existing institutional arrangements if new policies are to succeed.

European Neighbourhood Policy: Economic Review of EU Neighbour Countries

EUROPEAN ECONOMY, OCCASIONAL PAPERS, No 30, June 2007, European Commission. ISBN 978-92-79-04688-9

This is the third issue of the Economic Review of EU Neighbour Countries. The European neighbourhood runs from Morocco in North Africa, through the Middle East, to Russia – including those countries that directly border, or are close to the European Union, and whose growth and welfare is of particular importance to Europe for economic and political reasons. This year the review includes a special focus on a topical issue: the macroeconomic effects of energy price shocks in resource-poor CIS countries (written in collaboration with the EBRD). After several years of below market prices for its gas exports to the CIS, Russia has decided to review these arrangements and to significantly increase prices, bringing them closer to the levels applied to the EU. Starting in early 2006 with Ukraine, the renegotiation of gas prices has also affected Armenia, Belarus, Georgia and Moldova. This chapter compares the macroeconomic effects of the energy-price shock on growth, macroeconomic stability, budget and balance of payments in these energy-importing countries. ■

The Directorate 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:

- European Economy. "Labour market and wage developments in 2006"
- European Economy. Economic Papers. "Tax revenues in the EU: recent trends and challenges ahead"
- European Economy. Occasional Papers. "2006 Economic and fiscal programmes of potential candidate countries"

KC-AJ-07-007-EN-C

For your diary

Euro changeover conference
1 October 2007, Malta

EMU governance and euro changeover: Malta on the path to the adoption of the euro

Hosted by the government of Malta with support from the Commission and the ECB, this conference will look at the policy challenges for the management of EMU at national and EU levels. Workshops will consider the practical aspects of the changeover to the euro, including the preparations, the euro and inflation, and the advantages for business and consumers. Prime Minister Lawrence Gonzi will give the opening address, and speakers will include Commissioner Almunia, ECB and DG ECFIN staff as well as European Parliamentarians.

Valletta – a lighthouse on the path to the euro

DG ECFIN research conference
11-12 October 2007, Brussels

Growth and income distribution in an integrated Europe: does EMU make a difference?

This annual ECFIN research conference will answer questions on the complex links between growth and income distribution in an increasingly integrated EU. How is wealth distribution changing? What factors are driving changes? Does EMU make a difference? And more. The conference will feature Anthony Atkinson of Oxford University, Giuseppe Bertola from the University of Turin, Cecilia Garcia Peñalosa of the CNRS and GREQAM Marseille, and Northwestern University's Robert J. Gordon as keynote speakers, and will include academic and practising economists contributing original work on these issues. For more information, see events on the DG ECFIN website.


Brussels – the royal palace

ECFIN conference
25 October 2007, Brussels

SMEs and the euro

This conference, organised by ECFIN together with partner associations, will discuss the challenges that SMEs face in prepaing for the introduction of the euro. Lessons drawn from earlier changeovers will be discussed, and good practice presented. The conference will also look at the impacts the euro has so far had on SMEs, including the benefits and opportunities it offers and the new ways of doing business it brings to the millions of small entrepreneurs in the EU. Speakers will be drawn from industry, various Commission DGs, and those Member States with recent experience in preparations for the euro. For more information, see the 'events' section of the DG ECFIN website.

DG ECFIN workshop
30 November 2007, Brussels

Achieving and safeguarding sound fiscal positions

Taking the SGP as the context, this workshop aims to improve understanding of the determinations and tools related to achieving a sound fiscal position, and then keeping it. Topics will cover: the lessons from past successes, the political and institutional settings that support the effective implementation of budgets and the role of medium-term budgetary frameworks, and the arrangements that give incentives to use the good times well and avoid pro-cyclical policies. For more information, see 'events' on the DG ECFIN website.

ECB workshop
30 November to 1 December 2007, Frankfurt

Forecast uncertainty in macroeconomics and finance

This fifth ECB workshop on forecasting techniques will present recent theoretical and empirical contributions on forecast uncertainty in the areas of macroeconomics and finance. The assessment of forecasts is of particular interest to those who use them, and who are confronted with the need to evaluate the importance of forecasts from different sources and models. For more information, see events on the ECB website. http://www.ecb.eu


Frankfurt – river banks and central banks

European Commission conference
March 2008, Brussels

Public finances in the EU

The European Commission, through its Bureau for European Policy Advisers (BEPA), will organise a major academic conference that will focus on the economic aspects of EU budgetary spending and financing, from the perspective of the long-run development of how the EU is funded. Issues to be covered include: the main factors affecting EU policy priorities, the assignment of policy responsibilities between EU, national and regional levels, possible EU taxes, and decision-making on the budget. For more information, see the BEPA website. http://ec.europa.eu/dgs/policy_advisers/index_en.htm or the 'events' section of the DG ECFIN website.

Further information

A list of the events organised by ECFIN is available at:
http://ec.europa.eu/economy_finance/events_en.htm

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