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EUROPEAN COMMISSION

DIRECTORATE-GENERAL FOR ECONOMIC
AND FINANCIAL AFFAIRS



**The broad economic policy guidelines
(for the 2005–08 period)**

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European Commission

EUROPEAN ECONOMY

Directorate-General for Economic and Financial Affairs

2005

Number 4

**The broad economic policy
guidelines
(for the 2005–08 period)**

Abbreviations and symbols used

Member States

BE	Belgium
CZ	Czech Republic
DK	Denmark
DE	Germany
EE	Estonia
EL	Greece
ES	Spain
FR	France
IE	Ireland
IT	Italy
CY	Cyprus
LV	Latvia
LT	Lithuania
LU	Luxembourg
HU	Hungary
MT	Malta
NL	The Netherlands
AT	Austria
PL	Poland
PT	Portugal
SI	Slovenia
SK	Slovakia
FI	Finland
SE	Sweden
UK	United Kingdom

EUR-12	European Union Member States having adopted the single currency (BE, DE, EL, ES, FR, IE, IT, LU, NL, AT, PT, FI)
EU-25	European Union, 25 Member States
EU-15	European Union, 15 Member States before 1 May 2004 (EUR-12 plus DK, SE and UK)
AC-10	European Union, 10 Member States that joined the EU on 1 May 2004 (CZ, EE, CY, LV, LT, HU, MT, PL, SI, SK)

Currencies

EUR	euro
ECU	European currency unit
DKK	Danish krone
GBP	Pound sterling
SEK	Swedish krona
CAD	Canadian dollar
CHF	Swiss franc
JPY	Japanese yen
SUR	Russian rouble
USD	US dollar

Other abbreviations

SCPs	Stability and convergence programmes
PEPs	Pre-accession economic programmes
NMS	New Member States
SGP	Stability and Growth Pact

Contents

The broad guidelines of the economic policies of the Member States and the Community (for the 2005–08 period) drawn up in conformity with Article 99(2) of the Treaty establishing the European Community

- 1. Introduction**
- 2. Commission recommendation of 12 April 2005**
- 3. European Parliament resolution of 26 May 2005 on the Commission recommendation**
- 4. Council recommendation of 12 July 2005**

The broad guidelines of the economic policies of the Member States and the Community (for the 2005–08 period)

drawn up in conformity with Article 99(2)
of the Treaty establishing the
European Community

Contents

1. Introduction	7
2. Commission recommendation of 12 April 2005 on the broad guidelines of the economic policies of the Member States and the Community (for the 2005–08 period)	11
Section A. Macroeconomic policies for growth and jobs	13
A.1. Macroeconomic policies creating the conditions for more growth and jobs	13
A.2. Ensuring a dynamic and well-functioning euro area	15
Section B. Microeconomic reforms to raise Europe’s growth potential	17
B.1 Making Europe a more attractive place to invest and work	17
B.2 Knowledge and innovation for growth	19
3. European Parliament resolution of 26 May 2005 on the Commission recommendation on the broad guidelines of the economic policies of the Member States and the Community in the framework of the integrated guidelines for growth and jobs (for the 2005–08 period)	23
4. Council recommendation of 12 July 2005 on the broad guidelines of the economic policies of the Member States and the Community (for the 2005–08 period)	35
Introduction	37
Section A. Macroeconomic policies for growth and jobs	39
A.1. Macroeconomic policies creating the conditions for more growth and jobs	39
A.2. Ensuring a dynamic and well-functioning euro area	41
Section B. Microeconomic reforms to raise Europe’s growth potential	44
B.1 Knowledge and innovation — engines of sustainable growth	44
B.2 Making Europe a more attractive place to invest and work	47

1. Introduction

The Spring European Council of 22 and 23 March 2005 concluded that five years after the launch of the Lisbon strategy not enough progress had been made in implementing the strategy. It called for urgent action and therefore decided to relaunch the strategy without delay and refocus priorities on growth and employment in line with the proposals made by the Commission ⁽¹⁾. The new start of the Lisbon strategy extended to improvements of the governance of the strategy with the aim of increasing the Member States' involvement and ownership of the reform process and simplifying and streamlining the reporting and monitoring procedures.

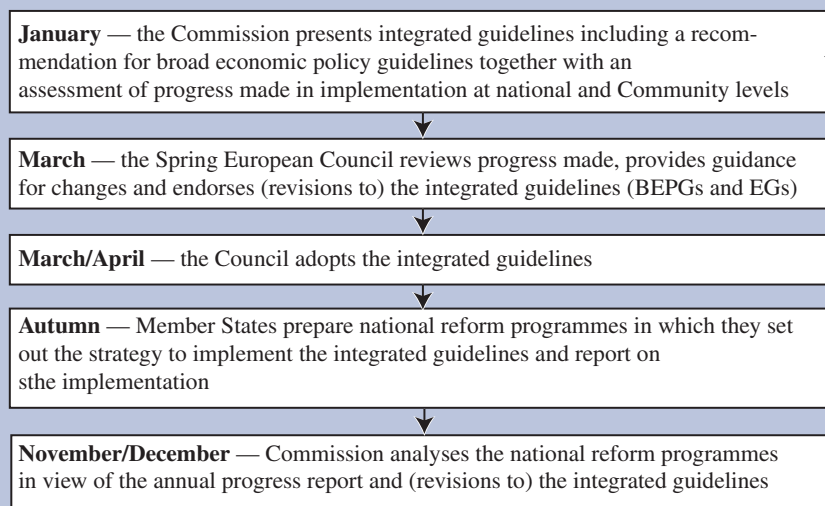
The refocusing of priorities is mirrored in the broad economic policy guidelines for the period 2005–08. Compared to the broad economic policy guidelines published in previous issues of the European Economy, a number of changes in relation to the revised governance framework can be highlighted. Firstly, to improve the coherence between the broad economic policy guidelines (BEPGs) and the employment guidelines (EGs), these two Treaty-based instruments for economic policy coordination have been merged into a set of integrated guidelines ⁽²⁾. As the EC Treaty lays down different proce-

dures for adoption of the BEPGs and the EGs, both sets of guidelines remain separate but at the same time mutually consistent and coherent. On the basis of the integrated guidelines adopted by the Council, the Member States will prepare national reform programmes setting out a comprehensive three-year strategy to implement the guidelines, while the Commission will prepare a Community Lisbon programme focusing exclusively on the actions to be undertaken at Community level. The assessment of these programmes will be reflected in the Commission's annual progress report. Secondly, the BEPGs for 2005–08 do not contain a country-specific part. In order to foster ownership and legitimacy at national level, it was considered that the guidelines should leave Member States the room to develop the appropriate policy mixes to cater for their own national specificities.

Thirdly, the calendar of the coordination cycle has been amended. Instead of presenting a Commission recommendation on the BEPGs shortly after the Spring European Council in March, the new coordination cycle envisages the Commission to come forward with these recommendations simultaneously with the assessment of the national reform programmes. In the context of the three-year cycle 2005–08, the Commission will present in the intermediate years 2006 and 2007, if necessary, updates of the guidelines in January.

⁽¹⁾ Commission communication, 'Working together for growth and jobs — a new start for the Lisbon strategy', COM (2005) 24, adopted on 2 February 2005.
⁽²⁾ Commission communication, 'Integrated guidelines for growth and jobs (2005–08)', COM (2005) 141 final, adopted on 12 April 2005.

Diagram 1: The new annual governance cycle following the mid-term review of the Lisbon strategy



2. Commission recommendation of 12 April 2005 on the broad guidelines of the economic policies of the Member States and the Community (for the 2005–08 period)

drawn up in conformity with Article 99(2)
of the Treaty establishing the European
Community

Section A. Macroeconomic policies for growth and jobs ⁽¹⁾

A.1 Macroeconomic policies creating the conditions for more growth and jobs

Securing economic stability to raise employment and growth potential

Sound macroeconomic policies are essential to support a well-balanced economic expansion and the full realisation of current growth potential. They are also vital for establishing framework conditions that will promote adequate levels of savings and investment, as well as a stronger orientation of the latter towards knowledge and innovation, so as to position the economy on a sustained, higher, non-inflationary, growth and employment path. In planning for the future, firms and individuals must have confidence that price stability will be maintained, and that exchange rates and long-term interest rates will be reasonably stable.

Monetary policies can contribute by pursuing price stability and, subject to this being achieved, by supporting other general economic policies. For some of the new Member States, it will be important that monetary policies allow a further decline in long-term interest rates and an exchange rate regime that is directed towards achieving sustainable real — and nominal — convergence. Eventual participation in European exchange-rate mechanism (ERM) II will help to strengthen those endeavours. An additional macroeconomic policy challenge for some of these Member States is to keep relatively high current account deficits within the range where sound external financing can be secured. In this respect, fiscal restraint will be essential to reduce current account deficits, as financing such deficits could become more difficult once privatisation is completed.

Securing a sound budgetary position will allow the full and symmetric play of the automatic budgetary stabilisers with a view to stabilising output around a higher and sustainable growth trend. For those Member States that have already achieved sound budgetary positions, the challenge is to retain that position without recourse to one-off and temporary measures. For the remaining Member States it is vital to take the necessary action to achieve their medium-term budgetary objectives in particular as economic conditions improve, thus avoiding pro-cyclical policies and putting themselves in a position in which sufficient room for the full play of automatic stabilisers is ensured prior to the next economic downturn. For individual Member States, the medium-term budgetary objective varies depending on the current debt ratio and potential growth, while preserving sufficient margin below the reference value of 3 % of GDP.

Guideline. To secure economic stability, Member States should maintain their medium-term budgetary objectives over the economic cycle and, as long as this objective has not yet been achieved, take all the necessary corrective measures in line with the Stability and Growth Pact. Subject to this, Member States should avoid pro-cyclical fiscal policies. Member States posting current account deficits that risk being unsustainable should work towards correcting them by implementing structural reforms to boost external competitiveness and also contribute to their correction via fiscal policies (Integrated guideline No 1).

⁽¹⁾ In implementing the policy guidelines set out below, Member States should note that the country-specific recommendations issued in the context of the Council recommendation of 26 June 2003 on the broad guidelines of the economic policies of the Member States and the Community (for the 2003–05 period) as completed and updated in the context of the Council recommendation of 5 July 2004 on the 2004 update of these guidelines, remain valid as background references.

**Safeguard long-term economic sustainability
in the light of Europe’s ageing population**

Europe’s ageing population poses serious risks to the long-term sustainability of the European Union (EU) economy. According to the latest projections, by 2050 the EU’s population of working age (15–64) will be 18 % lower than in 2000 and the number of people aged over 65 years will have increased by 60 %. This not only implies higher dependency ratios, it also means that there will be an increased debt burden, higher real interest rates and lower potential output unless action is taken now to safeguard the long-term sustainability of the EU economy.

Member States can address the economic implications of ageing by pursuing a faster pace of debt reduction and by taking measures to raise employment rates and increase labour supply so as to offset the impact of future declines in the number of persons of working age. It is also essential to modernise social protection systems so as to ensure that they are financially viable, while at the same time ensuring that they fulfil their goals in terms of access and adequacy, in the face of higher dependency ratios and the rising needs linked to an increase in the number of elderly persons. In particular, improved interaction between social protection systems and labour markets can remove distortions affecting retirement decisions and encourage extended working lives against a background of increased life expectancy.

Guideline. To safeguard economic sustainability Member States should, in view of the projected costs of ageing populations, undertake a satisfactory pace of government debt reduction to strengthen public finances, reform pension and healthcare systems to ensure that they are financially viable while being socially adequate and accessible, and take measures to raise employment rates and labour supply (Integrated guideline No 2). See also integrated guideline ‘Promote a lifecycle approach to work’ (No 17).

**Promote an efficient allocation of resources
and coherent macroeconomic and structural policies**

Well-designed tax and expenditure systems that promote an efficient allocation of resources are a necessity

for the public sector to make a full contribution towards growth and employment, without jeopardising the goals of economic stability and sustainability. This can be achieved by redirecting expenditure towards growth-enhancing categories such as research and development (R & D), physical infrastructure, human capital and knowledge. Member States can also help to control other expenditure categories through the use of expenditure rules and performance budgeting and by putting mechanisms in place to ensure that individual reform measures and overall reform packages are well designed. A key priority for the EU economy is to ensure that tax structures and their interaction with benefit systems promote higher growth potential through more employment and investment.

Guideline. To promote an efficient allocation of resources Member States should, without prejudice to guidelines on economic stability and sustainability, direct the composition of public expenditure towards growth-enhancing categories, adapt tax structures to strengthen growth potential and ensure that mechanisms are in place to assess the relationship between public spending and the achievement of policy objectives and ensure the overall coherence of reform packages (Integrated guideline No 3).

The role of sound macroeconomic policies is to provide conditions conducive to employment creation and growth, but ultimately it is structural reforms to promote efficient markets and well-designed public interventions that determine sustainable growth in output and welfare. A failure on the part of structural policies to deliver higher growth will undermine macroeconomic stability, for example, through budget deficits, persistent inflationary pressures and a lack of adjustment capacity in the face of temporary or permanent economic shocks. A key feature of Member States’ overall economic strategy is to ensure that they have a consistent set of structural policies that support the macroeconomic framework and vice versa. In particular, market reforms need to improve the overall adaptability and adjustment capacity of economies in response to changes in cyclical economic conditions and also longer term trends such as globalisation and technology.

Guideline. To promote greater coherence between macroeconomic and structural policies

Member States should pursue reforms that support the macroeconomic framework by increasing flexibility, mobility and adjustment capacity in response to globalisation, technological advances and cyclical changes (Integrated guideline No 4). See also integrated guideline 'Promote flexibility combined with employment security and reduce labour market segmentation' (No 20).

Ensure that wage developments contribute to macroeconomic stability and complement structural reforms

Wage developments can contribute to stable macroeconomic conditions and an employment-friendly policy mix provided that real wage increases are in line with the underlying rate of productivity growth over the medium term and are consistent with a rate of profitability that allows for productivity, capacity and employment-enhancing investment. This requires that temporary factors such as increases in productivity caused by a cyclical rebound or one-off rises in the headline rate of inflation do not cause an unsustainable trend in wage growth and that wage developments reflect local labour market conditions.

Given the continued upward pressure on oil and raw material prices, vigilance is needed over the impact of wage settlements and labour-cost increases on price competitiveness. Efforts can be made at EU level to foster continued dialogue and information exchange between monetary and fiscal authorities and the social partners via the macroeconomic dialogue.

Guideline. To ensure that wage developments contribute to macroeconomic stability and growth

and to increase adaptability, Member States should promote nominal wage increases and labour costs consistent with price stability and the trend in productivity over the medium term, taking into account differences across skills and local labour market conditions (Integrated guideline No 5). See also integrated guideline 'Ensure employment-friendly wage and other labour-cost developments' (No 21).

A.2 Ensuring a dynamic and well-functioning euro area

The need to achieve higher growth and employment is particularly acute in the euro area given its recent subdued economic performance and its low level of potential growth of around 2 % (Commission estimates). Domestic demand has been particularly muted in the euro area, with both private consumption and investment significantly below that of the EU-25 as a whole in 2004. Muted private consumption seems to be rooted in continuing concerns regarding employment prospects (with unemployment continuing to be around 9 %), the sustainability of pensions systems and public finances more generally and income prospects in the medium term.

The challenge for the euro area is to ensure the realisation of current growth potential and even more to raise its growth potential over time. This is best achieved through growth and stability-oriented macroeconomic policies and comprehensive structural reforms. Both are also particularly salient for euro-area Member States as they have an important impact on their capacity to adequately adjust to shocks with an asymmetric impact and therefore on the economic resilience of the euro area as a whole. Furthermore, the economic performance of, and policies pursued by, individual euro-area Member States affect common goods such as the euro's exchange rate, interest rates and price stability. All this implies a need for stronger macroeconomic and structural policy coordination in the euro area.

Economic and monetary union (EMU) places a particular premium on safeguarding fiscal discipline to protect such common goods. The absence of national interest and exchange-rate policies implies also an increased need to achieve and maintain sound budget positions which provide sufficient budgetary margin to absorb the impact of cyclical fluctuations or economic shocks with an asymmetric impact.

Structural policies that foster the smooth adjustment of prices and wages are essential to ensure that euro-area Member States have the capacity to rapidly adjust to shocks (such as the current oil-price shock) and to help to reduce unwarranted inflation differences between Member States. Policies that increase the responsiveness of labour markets, through encouraging widespread labour participation, occupational and geographical mobility and the setting of wages, together with reforms

*The broad economic policy guidelines
(for the 2005–08 period)*

that enhance product market flexibility are particularly important in this respect.

To contribute to international economic stability and better represent its economic interests, it is critical for the euro area to play its full role in international monetary and economic policy cooperation. Whilst the creation of a stable Eurogroup Presidency will help to coordinate euro-area members' positions, the external representation of the euro area remains fragmented and incomplete, preventing the euro area from taking a leading strategic role in the development of the global economic system.

Guideline. To contribute to a dynamic and well-functioning EMU, euro-area Member States need to pay particular attention to fiscal discipline, and in this connection, those that have not yet reached their medium-term budgetary objective should pursue an annual improvement in their cyclically-adjusted budget deficit net of one-offs and other temporary measures of 0.5 % of GDP as a benchmark, while ensuring a higher adjustment effort in good times; press forward with structural reforms that will improve euro-area competitiveness and economic adjustment to asymmetric shocks; and ensure that the euro-area's influence in the global economic system is commensurate with its economic weight (Integrated guideline No 6).

Section B. Microeconomic reforms to raise Europe's growth potential

Structural reforms are essential to increase the EU's growth potential, because they increase the efficiency and adaptability of the European economy. To yield maximum synergies, they are best implemented in a comprehensive and coordinated way.

Raising Europe's growth potential requires making progress in both job creation and productivity growth. Since the mid-1990s, productivity growth in the EU has slowed down markedly. Reversing this trend is the major competitiveness challenge facing the Union, especially in the light of its ageing population. Population ageing alone is estimated to reduce by nearly half the current rate of potential growth. An acceleration of productivity growth is thus indispensable to maintain and increase future living standards.

Productivity gains are fuelled by investment and innovation. Making Europe a more attractive investment location and spurring investment in knowledge and innovation are therefore key elements of the Lisbon Action Programme agreed at the 2005 Spring European Council. This is why national and regional programmes supported by the Structural Funds and the Cohesion Fund will be increasingly targeted on investments in these fields in accordance with the Lisbon objectives.

B.1 Making Europe a more attractive place to invest and work

The attractiveness of the European Union as an investment location depends *inter alia* on the size and openness of its markets, its regulatory environment and the quality of its infrastructure. Increased investment will make Europe more productive as labour productivity levels depend on investment in physical and human capital as well as in knowledge and infrastructure.

Extend and deepen the internal market

The ability of European producers to compete and survive in the internal market is key to their competitive strength in world markets. A fully integrated internal market would also make the EU more attractive to foreign investors. Whilst the internal market for goods is relatively well integrated, services markets remain, legally or *de facto*, rather fragmented. This applies in particular to energy and transport markets and to the regulated professions. In order to promote growth and employment and to strengthen competitiveness, the internal market of services has to be fully operational while preserving the European social model. The elimination of tax obstacles to cross-border activities and the removal of remaining impediments to worker mobility would also bring important efficiency gains. Finally, the full integration of financial markets would raise output and employment by allowing more efficient allocation of capital and creating better conditions for business finance.

Guideline. To extend and deepen the internal market, Member States should speed up the transposition of internal market directives, give priority to stricter and better enforcement of internal market legislation, accelerate the process of financial market integration, eliminate tax obstacles to cross-border activities and apply EU public-procurement rules effectively (Integrated guideline No 7).

Despite general acknowledgement of the potential benefits of a single European market, the transposition rate of internal market directives remains disappointingly low.

Furthermore, directives are often not implemented or applied correctly, as illustrated by the high number of infringement proceedings launched by the Commission. Member States need to cooperate more positively with each other and with the Commission to ensure that they deliver the full benefits of internal market legislation to their citizens and businesses. For example, there is considerable scope for further improvements in public-procurement practices. Such improvements would be reflected in an increase in the share of public procurement publicly advertised. Moreover, more open procurement would lead to significant budgetary savings for the Member States.

Ensure open and competitive markets inside and outside Europe

Open and competitive markets contribute to more efficient use of resources, lead to better organisation of work within companies, and can act as a stimulus to innovation. Competition policy has played a key role in ensuring a level playing field for firms in the EU, and can also be instrumental to look at the wider regulatory framework around markets, in order to promote the conditions which will allow firms to compete effectively. A further opening up of European markets to competition can be

Guideline. To ensure open and competitive markets, Member States should give priority to the removal of regulatory and other barriers that hinder competition in key sectors; a more effective enforcement of competition policy; selective market screening by competition and regulatory authorities in order to identify and remove obstacles to competition and market entry; a reduction in State aid that distorts competition; and a redeployment of aid in favour of support for certain horizontal objectives such as research and innovation and the optimisation of human capital. Member States should also fully implement the agreed measures to open up the network industries to competition in order to ensure effective competition in European-wide integrated markets, allowing at the same time to guarantee the satisfactory delivery of high-quality services of general economic interest (Integrated guideline No 8).

achieved by a reduction in the general level of State aid, while making allowance for genuine market failures. This movement must be accompanied by a redeployment of remaining State aid in favour of support for certain horizontal objectives such as research and innovation and the optimisation of human capital.

Structural reforms that ease market entry are a particularly effective tool for enhancing competition. These will be particularly important in markets that were previously sheltered from competition because of anti-competitive behaviour, over-regulation (permits, licences, minimum capital requirements, legal barriers, shop opening hours, regulated prices, limited sales periods, etc.), or because of trade protection. The Council has already invited Member States to screen existing domestic legislation for compatibility with EU rules in order to remove market barriers and open up competition in the internal market.

In addition, the implementation of measures already agreed to open up the network industries to competition should help to ensure lower prices overall and greater choice while guaranteeing the delivery of services of general economic interest to all citizens. Competition and regulatory authorities should ensure sufficient competition in liberalised markets, where the market share of the incumbent often remains very high.

Guideline. To create a more attractive business environment, Member States should improve the quality of their regulations through a systematic and rigorous assessment of their economic, social and environmental impacts, while taking into consideration the administrative costs associated with regulation. Moreover, Member States should consult widely on the costs and benefits of their regulatory initiatives, in particular where these imply trade-offs between different policy objectives (Integrated guideline No 9).

A common approach in dealing with third countries is essential so as to improve market access conditions for EU firms. The successful completion of an ambitious agreement in the framework of the Doha Round should

further open up world markets to trade and investment, thus contributing to raising potential growth.

Improve European and national regulations

Market regulation is essential to create a low-cost environment in which commercial transactions can take place. It also serves to correct market failures or to protect market participants. Nevertheless, the cumulative impact of regulations may impose substantial economic costs. It is therefore essential that regulations are well designed and proportionate.

When preparing or revising legislation, Member States should systematically assess the costs and benefits of their legislative initiatives. This implies consultation of relevant stakeholders, while allowing them sufficient time to respond. Member States are invited to develop better national regulation agendas and report on these in their national Lisbon programmes.

Guideline. To promote a more entrepreneurial culture and create a supportive environment for SMEs, Member States should improve access to finance, adapt tax systems, strengthen the innovative potential of SMEs, and provide relevant information and support services in order to encourage the creation and growth of start-ups in line with the SMEs charter. In addition, Member States should reinforce entrepreneurship education and training (cross reference to the relevant employment guideline). Member States should also facilitate the transfer of ownership, revise their bankruptcy laws, and improve their rescue and restructuring proceedings (Integrated guideline No 10).

In the Commission's approach to better regulation, the economic, social and environmental impacts of new or revised regulations are carefully assessed to identify the potential trade-offs and synergies between different policy objectives. Moreover, existing regulation is screened for simplification potential and its impact on competitiveness is assessed. Finally, a common approach to measuring the administrative costs of new and existing legislation is being developed.

Significant improvements in the regulatory environment can therefore be achieved by reducing the costs associated with regulation, including administrative costs. This is especially important for small and medium-sized enterprises (SMEs), which usually have only limited resources to deal with the administration imposed by both Community and national legislation.

Europe needs to foster its entrepreneurial drive more effectively and it needs more new firms willing to embark on creative or innovative ventures. Learning about entrepreneurship through all forms of education and training, should be supported and relevant skills provided. To this end, partnerships with companies should be encouraged. The creation and growth of businesses can also be encouraged by improving access to finance, adopting tax systems to reward success and providing business support services, notably for young entrepreneurs. Particular emphasis should be put on facilitating the transfer of ownership, revising bankruptcy laws, and improving rescue and restructuring proceedings.

Expand and improve European infrastructure

Modern infrastructure is an important factor affecting the attractiveness of locations. It facilitates the mobility of persons, goods and services throughout the Union. Modern transport, energy and electronic communication infrastructure is a prerequisite for reaping the benefits of a re-invigorated Lisbon strategy. By reducing transport costs and by widening markets, interconnected and interoperable trans-European networks help foster international trade and fuel internal market dynamics. Moreover, the ongoing liberalisation of European network industries fosters competition and drives efficiency gains in these sectors.

In terms of future investment in European infrastructure, the implementation of 30 priority transport projects identified by Parliament and Council in the trans-European network (TEN) transport guidelines as well as the implementation of the quick-start cross-border projects for transport, energy and broadband communications identified under the European initiative for growth should be considered a priority. Infrastructure bottlenecks within countries need to be tackled as well. Appropriate infrastructure pricing systems can contribute to the efficient use of infrastructure and the development of a sustainable modal balance.

Guideline. To expand and improve European infrastructure and complete agreed priority cross-border projects with the particular aim of achieving a greater integration of national markets within the enlarged EU. Member States should develop adequate transport, energy or ICT infrastructures, notably in cross-border sections, as an essential condition to achieve a successful opening-up of the network industries to competition. In addition, they should introduce appropriate infrastructure pricing systems, as a means to internalise environmental costs to ensure the efficient use of infrastructures and the development of a sustainable modal balance (Integrated guideline No 11).

B.2 Knowledge and innovation for growth

Knowledge accumulated through investment in R & D, innovation and education is a key driver of long-run growth. Policies aimed at increasing investment in knowledge and strengthening the innovation capacity of the EU economy are at the heart of the Lisbon strategy for growth and employment.

Increase and improve investment in R & D

R & D affects economic growth through various channels: first, it can contribute to the creation of new markets or production processes; second, it can lead to incremental improvements in already existing products and production processes; and third, it increases the capacity of a country to absorb new technologies.

The EU is currently spending around 2 % of GDP on R & D (although ranging from below 0.5 % to above 4 % of GDP across Member States), barely up from the level at the time of the launch of the Lisbon strategy. Moreover, only around 55 % of research spending in the EU is financed by industry. More rapid progress towards meeting the collective EU target of raising research investment to 3 % of GDP is needed; two thirds of the overall investment should come from the private sector. Member States are invited to report on their R & D expenditure targets for 2008 and 2010 and the measures to achieve these in their national Lisbon programmes. The main challenge is to put in place framework conditions, instruments and incentives for companies to invest

in research. Public research expenditure must be made more effective and the links between public research and the private sector have to be improved. Poles and networks of excellence should be strengthened and better use should be made of public-support mechanisms including fiscal measures to leverage private R & D. It is also essential to ensure that companies operate in a sufficiently competitive environment since competition provides an important incentive to private spending on innovation. In addition, a determined effort must be made to increase the number and quality of researchers active in Europe, in particular by attracting more students into scientific, technical and engineering disciplines, and enhancing the career development and the transnational and intersectoral mobility of researchers.

Guideline. To increase and improve investment in R & D, Member States should further develop the mix of measures to foster business R & D through: improved framework conditions and ensuring that companies operate in a sufficiently competitive environment; increased and more effective public expenditure on R & D; strengthening centres of excellence; making better use of support mechanisms, such as fiscal measures to leverage private R & D; ensuring a sufficient supply of qualified researchers by attracting more students into scientific, technical and engineering disciplines and enhancing the career development and the transnational and intersectoral mobility of researchers (Integrated guideline No 12). See also integrated guideline 'Expand and improve investment in human capital' (No 22).

Facilitate innovation, the uptake of ICT and the sustainable use of resources

The dynamism of the European economy is crucially dependent on its innovative capacity. The economic framework conditions for innovation need to be in place. This implies well-functioning financial and product markets as well as clearly-defined and affordable intellectual property rights. Innovations are often introduced to the market by new enterprises, which may meet particular difficulties in obtaining finance. Measures to encourage the creation and growth of innovative enterprises, including improving access to finance, should

therefore enhance innovative activity. Technology diffusion can be fostered by the development of innovation poles and networks as well as by innovation support services targeted at SMEs. Knowledge transfer via researcher mobility, foreign direct investment (FDI) or imported technology is particularly beneficial for lagging countries and regions.

The EU has been unable to reap the full benefits of the increased production and use of information and communication technologies (ICT). This reflects the still continuing under-investment in ICT, institutional constraints and organisational challenges to the adoption of ICT. Technological innovation ultimately depends on a growth-conducive economic environment. Uptake of ICTs particularly depends on an adaptable organisation of work and flexible markets.

Guideline. To facilitate innovation and the uptake of ICT, Member States should focus on improvements in innovation support services, in particular for technology transfer, the creation of innovation poles and networks bringing together universities and enterprises, the encouragement of knowledge transfer through FDI, better access to finance and affordable and clearly-defined intellectual property rights. They should facilitate the uptake of ICT and related changes in the organisation of work in the economy (Integrated guideline No 13).

Lasting success for the Union also depends on addressing a range of resource and environmental challenges which, if left unchecked, will act as a brake on future growth. In this context, recent developments and prospects on oil prices have emphasised the acuity of the energy-efficiency issue. Further delay in addressing these challenges would raise the economic costs of taking action. This implies, for example, measures to tackle the problem of climate change, to make more rational use of resources and to halt the loss of biodiversity. The use of market-based instruments, so that prices better reflect environmental damage and social costs, plays a key role in this context. Encouraging the development and use of environment-friendly technologies and the greening of public procurement can improve the innovative performance and

enhance the contribution to sustainable development of the sectors concerned. For example, EU companies are amongst the world leaders in developing new renewable energy technologies. In particular, in a context of continued upward pressure on energy prices, and accumulating threats to the climate, it is important to push energy-efficiency improvements as a contribution to both sustainable development and competitiveness.

Guideline. To encourage the sustainable use of resources and strengthen the synergies between environmental protection and growth, Member States should give priority to the internalisation of external environmental costs; to increasing energy efficiency and to the development and application of environment-friendly technologies. The implementation of these priorities should be in line with existing European commitments and with the actions and instruments proposed in the Environmental Technologies Action Plan (ETAP), through the use of market-based instruments, risk funds and R & D funding, greening of public procurement and the removal of environmentally harmful subsidies alongside other policy instruments (Integrated guideline No 14).

Contribute to a strong European industrial base

The recent slowdown in EU productivity growth is partly related to the EU's difficulty in re-orienting its economy towards the newer, higher productivity growth sectors. In order to enhance and sustain economic and technological leadership, Europe must increase its capacity to develop and market new technologies. The synergies from jointly addressing research, regulatory and financing challenges at European level, where for reasons of scale or scope individual Member States cannot successfully tackle market failures in isolation, have not always been fully exploited, programmes such as Galileo or those in the aeronautics industry being exceptions. As a result, the EU has been unable to fully realise its technological potential. The pooling of European excellence and the development of public-private partnerships where the benefits for society are larger than those for the private sector will help tap this potential.

***The broad economic policy guidelines
(for the 2005–08 period)***

Guideline. To contribute to a strong European industrial base, Member States should focus on the development of new technologies and markets. This implies in particular commitment to the setting up and implementation of joint European technology initiatives and public-private partnerships that help tackle genuine market failures, as well as the creation and development of regional or local clusters (Integrated guideline No 15).

**3. European Parliament
resolution of 26 May 2005
on the Commission
recommendation on the broad
guidelines of the economic policies
of the Member States and the
Community in the framework
of the integrated guidelines for
growth and jobs
(for the 2005–08 period)
(COM(2005)0141 —
2005/2017(INI))**

The European Parliament,

- having regard to the Commission recommendation (COM(2005)0141),
 - having regard to Article 99(2) of the EC Treaty,
 - having regard to the spring 2005 economic forecasts drawn up by the Commission for the euro area and the European Union (2005–06),
 - having regard to the conclusions of the Presidency of the Lisbon European Council of 23 and 24 March 2000, the Gothenburg European Council of 15 and 16 June 2001 and the Barcelona European Council of 15 and 16 March 2002,
 - having regard to the conclusions of the Presidency of the European Councils held in Brussels on 20 and 21 March 2003, 16 and 17 October 2003, 25 and 26 March 2004, 4 and 5 November 2004 and 22 and 23 March 2005,
 - having regard to its resolution of 22 February 2005 on the European economic situation — preparatory report on the broad economic policy guidelines,
 - having regard to Rule 107 of its Rules of Procedure,
 - having regard to the report of the Committee on Economic and Monetary Affairs (A6-0150/2005),
- A. whereas growth in the euro area and the 25-member European Union is failing to achieve its potential on a sustained basis and is still too weak, particularly in the four leading economies in the euro area; whereas household consumption is still faltering and the economic outlook for 2005 and 2006 continues to be unsatisfactory, contributing to a continuing high level of unemployment which will decline only slowly; whereas, despite the lowest interest rates since the Second World War, there is little willingness to invest;
- B. whereas structural reforms of product, energy and labour markets and taxation systems and the implementation of the internal market have not been carried out in all the Member States with the requisite care, and whereas reforms at Community level are making only slow progress;
- C. whereas the Stability and Growth Pact has contributed to maintaining a low level of inflation and a historically low level of interest rates;
- D. whereas worldwide competition is steadily increasing; whereas the European Union is lagging behind the growth rates in many other parts of the world and sees its market shares on third markets threatened; whereas the economic growth in the Union on average is lagging behind the United States as well as some key Asian economies;
- E. whereas the Lisbon strategy requires the mobilisation of all existing instruments, in particular the broad economic policy guidelines (BEPGs), the Seventh EU Framework Programme for Research (2007–13) and the Competitiveness and Innovation Framework Programme (2007–13), and the redirecting of expenditure towards growth-enhancing and job-creating categories in the framework of the financial perspective 2007–13;
- F. whereas the Lisbon process is part of the EU's strategy for sustainable development and whereas the environmental dimension must be an integral part of the European strategy to boost employment;
- G. whereas the Union is now an entity comprising 455 million men and women in 25 very disparate countries; whereas there are considerable economic and social disparities between and, in many cases, within the Member States; whereas the growth in a number of Member States is considerably higher than in others; whereas excessively general guidelines could fail to take account of the diversity of problems arising;
- H. whereas economic growth is not an objective in itself but part of an integrated approach focusing on the welfare and quality of life of citizens; whereas the pursuit of sustainable growth must be based on social, employment, environmental and budgetary policies which show a sense of responsibility towards future generations and respect for the different preconditions of the Member States;

*The broad economic policy guidelines
(for the 2005–08 period)*

- I. whereas unemployment is the greatest social injustice; whereas social cohesion can only be strengthened by growth in all parts of the Union, facilitating a high level of social protection and a high level of employment, in accordance with the objectives set out in the Treaty;
 - J. whereas growth can only be achieved through higher competitiveness and more investment; whereas the Union lags far behind its main competitors in the field of research and development, innovation and investing in the start-up of new enterprises;
1. Welcomes the presentation of integrated BEPGs and employment guidelines which concentrate on growth and employment while remaining committed to a balance between the three pillars of the Lisbon strategy in line with the presidency conclusions of the Brussels European Council of 22 and 23 March 2005, that integrated presentation being a sign of the complementary nature of economic and social policy and of commitment to further progress towards making the macroeconomic framework established for the Union simpler and easier to understand; supports the determination of the Council and the Commission to concentrate to a greater extent on growth and employment by increasing competitiveness, extending the internal market to the services sector, improving the efficiency of public services and consequently boosting domestic demand;
 2. Deplores the fact that the Commission's recommendations pay little attention to the environmental dimension in kick-starting growth and employment; recalls that environmental requirements will help to establish a forward-looking, dynamic and efficient economy which offers citizens a high quality of life;
 3. Stresses the importance of creating employment in the personal services and community services sector in a society of high female employment with an ageing and urbanised population; points to the importance of diversification and increased competition in a sector where it is important for citizens to enjoy the highest possible level of service and a range of choices, as such objectives also create opportunities for entrepreneurship for both women and men;
 4. Regrets the excessively general nature of the integrated guidelines, which do not take sufficient account of the differences between Member States; encourages the Commission in its plan to submit a communication identifying the key challenges for each of the Member States, especially in the field of structural reforms and investment as well as for more rapid exchange of advanced knowledge in setting economic policy;
 5. Recalls that a healthy macroeconomic environment implies adequate interaction between coordinated budgetary policies, an independent monetary policy that maintains the objective of price stability and further pursues the one of achieving the Union's general goals as enshrined in the Treaty, in an effort to reach better living standards and the objectives of sustainable development; calls on the Member States to implement structural reforms that help stimulate investment and therefore make full use of the low interest rates guaranteed by the ECB and to use the room for manoeuvre in the reformed Stability and Growth Pact to foster a more qualitative European economic growth, all of which underlines the opportunities and the need for increased trade in all sectors and the necessity to complete the single market;
 6. Highlights the attraction exerted by the European model and the major role of the Union and of the Member States in world trade; underlines the need for a labour market which is open to all citizens and flexible enough to help people opt into the market and which does not force older people willing to work out of their jobs;
 7. Stresses the necessity to restructure economic policy, focusing it on factors related to productivity growth, e.g. the modernisation of the economy, knowledge and social welfare and institutional arrangements, to meet the challenges of the recent enlargement and the requirements of a modern economy and resist the deflationary pressure of the third world;
 8. Notes that increased labour productivity, efforts to strengthen competitiveness, investment and growth are prerequisites for higher wages and an equitable distribution of the fruits of growth, employment and social cohesion; stresses that such

3. *European Parliament resolution of 26 May 2005
on the Commission recommendation*

a development should be followed by an obligation for enterprises to meet their social responsibilities;

9. Is of the view that increased and sustainable growth in Europe requires simultaneous, coordinated action by all Member States, including the completion of the internal market, a higher level of investment and innovative labour market reforms;

10. Regrets the conditions, in particular in terms of the timetable, under which Parliament is required to

express an opinion on the integrated guidelines; calls for the conditions relating to interinstitutional cooperation on the integrated guidelines to be clarified before the European Council in June 2005 in order to prevent this situation being repeated, while taking into account the consequences of the revision of the Lisbon strategy;

11. Calls on the Council to take account of the following modifications:

Commission recommendation

Modifications by Parliament

Modification 1

Section A, Chapter A.1, paragraph 4

Guideline. To secure economic stability, Member States should maintain their medium-term budgetary objectives over the economic cycle and, as long as this objective has not yet been achieved, take all the necessary corrective measures in line with the Stability and Growth Pact. Subject to this, Member States should avoid pro-cyclical fiscal policies. Member States posting current account deficits that risk being unsustainable should work towards correcting them by implementing structural reforms to boost external competitiveness and also contribute to their correction via fiscal policies (Integrated guideline No 1).

Guideline. To secure economic stability *in order to facilitate economic growth, and to transform a competitive advantage of diversity of cultural heritage and intellectual capital into innovation-driven growth in productivity*. Member States should maintain their medium-term budgetary objectives over the economic cycle and, as long as this objective has not yet been achieved, take all the necessary corrective measures in line with the Stability and Growth Pact. Subject to this, Member States should avoid pro-cyclical fiscal policies. Member States posting current account deficits that risk being unsustainable should work towards correcting them by implementing structural reforms to boost external competitiveness and also contribute to their correction via fiscal policies, *particularly by using the fruits of growth; moreover, Member States should redirect public spending towards budget categories that support the objectives of the Lisbon strategy, particularly investment aimed at developing human resources, knowledge, innovation and infrastructure, in order to assist economic development* (Integrated guideline No 1).

Commission recommendation

Modifications by Parliament

Modification 2

Section A, Chapter A.1, paragraph 7

Guideline. To safeguard economic sustainability Member States should, in view of the projected costs of ageing populations, undertake a satisfactory pace of government debt reduction to strengthen public finances, reform pension and healthcare systems to ensure that they are financially viable while being socially *adequate* and accessible, and take measures to raise employment rates and labour supply (Integrated guideline No 2). See also integrated guideline ‘Promote a lifecycle approach to work’ (No 17).

Guideline. To safeguard economic sustainability *as a basis for increased employment*, Member States should, in view of the projected costs of ageing populations *and taking account of the economic cycle*, undertake a satisfactory pace of government debt reduction to strengthen public finances, *reform tax systems, inter alia by reducing the burden on low wage earners, further reform* pension and healthcare systems to ensure that they are financially viable while being socially *satisfactory* and accessible, and take measures to raise *citizen’s responsibility for pension systems*, employment rates and *high-quality* labour supply (Integrated guideline No 2). See also integrated guideline ‘Promote a lifecycle approach to work’ (No 17).

Modification 3

Section A, Chapter A.1, paragraph 9

Guideline. To promote an efficient allocation of resources Member States should, without prejudice to guidelines on economic stability and sustainability, direct the composition of public expenditure towards growth-enhancing categories, adapt tax structures to strengthen growth *potential* and ensure that mechanisms are in place to assess the relationship between public spending and the achievement of policy objectives and ensure the overall coherence of reform packages (Integrated guideline No 3).

Guideline. To promote an efficient allocation of resources Member States should, without prejudice to guidelines on economic stability and sustainability, direct the composition of public expenditure towards growth-enhancing *and job-creating* categories *and adapt* tax structures to strengthen *potential* growth and *stimulate private investment, particularly by creating a fiscal framework that is favourable to SMEs and offers incentives to create jobs; Member States should cooperate to combat tax evasion; Member States should also* ensure that mechanisms are in place to assess the relationship between public spending and the achievement of policy objectives and ensure the overall coherence of reform packages (Integrated guideline No 3).

Commission recommendation

Modifications by Parliament

Modification 4

Section A, Chapter A.1, paragraph 11

Guideline. To promote greater coherence between macroeconomic and structural policies, Member States should pursue reforms that support the macroeconomic framework by increasing *flexibility*, mobility and adjustment capacity in response to globalisation, technological advances and cyclical changes (Integrated guideline No 4). See also integrated guideline 'Promote flexibility combined with employment security and reduce labour market segmentation' (No 20).

Guideline. To promote greater coherence between macroeconomic and structural policies, Member States should pursue reforms that support the macroeconomic framework by *maintaining strict fiscal procedures, stimulating investment and enterprise and fostering consumer confidence, and by further increasing adaptability*, mobility, *creativity* and adjustment capacity in response to *the challenges of* globalisation, technological advances and cyclical changes; *special attention must be given to the flexibility and security of the labour market*. (Integrated guideline No 4). See also integrated guideline 'Promote flexibility combined with employment security and reduce labour market segmentation' (No 20).

Modification 5

Section A, Chapter A.1, paragraph 14

Guideline. To ensure that wage developments contribute to macroeconomic stability *and* growth and to increase adaptability, Member States should promote nominal wage increases and labour costs consistent with *price stability and* the trend in productivity over the medium term, taking into account differences across skills and local labour market conditions (Integrated guideline No 5). See also integrated guideline 'Ensure employment-friendly wage and other labour-cost developments' (No 21).

Guideline. To ensure that wage developments contribute to macroeconomic stability, growth *and employment*, and to increase adaptability, Member States *and the social partners* should promote nominal wage increases and labour costs consistent with the trend in productivity over the medium term, taking into account differences across skills and local labour market conditions; *the fulfilment of the single market, labour market reforms and a strengthening of the social partners' responsibility for low unemployment by decentralised wage negotiations are crucial to increase wages and reduce differences in income, while remaining consistent with the evolution of productivity and competitiveness*. (Integrated guideline No 5). See also integrated guideline 'Ensure employment-friendly wage and other labour-cost developments' (No 21).

Commission recommendation

Modifications by Parliament

Modification 6

Section A, Chapter A.2, paragraph 6

Guideline. To contribute to a dynamic and well-functioning EMU, euro-area Member States need to pay particular attention to fiscal discipline, and in this connection those that have not yet reached their medium-term budgetary objective should pursue an annual improvement in their cyclically-adjusted budget deficit net of one-offs and other temporary measures of 0.5 % of GDP as a benchmark, while ensuring a higher adjustment effort in good times; press forward with structural reforms that will improve euro-area competitiveness and economic adjustment to asymmetric shocks; *and* ensure that the *euro area's influence* in the global economic system is commensurate with its economic weight (Integrated guideline No 6).

Guideline. To contribute to a dynamic and well-functioning EMU, euro-area Member States need to pay particular attention to fiscal discipline, *so as to ensure better coordination of their economic and budgetary policies, initially by harmonising their budgetary timetables*; and in this connection those *Member States* that have not yet reached their medium-term budgetary objective should pursue an annual improvement in their cyclically-adjusted budget deficit net of one-offs and other temporary measures of 0.5 % of GDP as a benchmark, while ensuring a higher adjustment effort in good times; *bearing in mind that, in future, structural reforms will be taken into account when defining the adjustment path to the medium-term objective, and temporary deviations from this objective will be allowed for countries that have already reached it*; press forward with structural reforms that will improve euro-area competitiveness *inter alia by investing in innovation, industrial policy, education and vocational training* and economic adjustment to asymmetric shocks; *Member States should complete the reform of the Stability and Growth Pact and ensure that it is strictly applied in order to re-establish confidence. Moreover, Member States should ensure the external representation of the euro area in accordance with the commitments made at the Vienna European Council of 11 and 12 December 1998, so that the increasingly important role of the euro in the global economic system is commensurate with its economic weight. In the new Member States, nominal convergence must be accompanied by real convergence.* (Integrated guideline No 6).

Commission recommendation

Modifications by Parliament

Modification 7

Section B, Chapter B.1, paragraph 4

Guideline. To extend and deepen the internal market, Member States should speed up the transposition of internal market directives, give priority to stricter and better enforcement of internal market legislation, accelerate the process of financial market integration, eliminate tax obstacles to cross-border activities and apply EU public-procurement rules effectively (Integrated guideline No 7).

Guideline. To extend and deepen the internal market, Member States should speed up the transposition of internal market directives, give priority to stricter and better enforcement of internal market legislation, accelerate the process of financial market integration, eliminate *bureaucratic and* tax obstacles to cross-border activities *by pressing forward with negotiations on harmonising the tax basis* and apply EU public-procurement rules effectively (Integrated guideline No 7).

Modification 8

Section B, Chapter B.1, paragraph 9

Guideline. To ensure open and competitive markets, Member States should give priority to the removal of regulatory and other barriers that hinder competition in key sectors; a more effective enforcement of competition policy; selective market screening by competition and regulatory authorities in order to identify and remove obstacles to competition and market entry; *a reduction in* State aid that distorts competition; and a redeployment of aid in favour of support for certain horizontal objectives such as research and innovation and the optimisation of human capital. Member States should also fully implement the agreed measures to open up the network industries to competition in order to ensure effective competition in European-wide integrated markets, allowing at the same time to guarantee the *satisfactory* delivery of high-quality services of general economic interest (Integrated guideline No 8).

Guideline. To ensure open and competitive markets, Member States should give priority to the removal of regulatory and other barriers that hinder competition in key sectors; a more effective enforcement of competition policy; selective market screening by competition and regulatory authorities in order to identify and remove obstacles to competition and market entry, *which are contrary to consumers' interests; the abolition of* State aid that distorts competition *inside the internal market*; and a redeployment of aid in favour of support for certain horizontal objectives such as research and innovation and the optimisation of human capital. Member States should also fully implement the agreed measures to open up the network industries to competition in order to ensure effective competition in European-wide integrated markets, allowing at the same time to guarantee the delivery of high-quality services of general economic interest (Integrated guideline No 8).

Commission recommendation

Modifications by Parliament

Modification 9

Section B, Chapter B.1, paragraph 14

Guideline. To create a more attractive business environment, Member States should improve the quality of their regulations through a systematic and rigorous assessment of their economic, social and environmental impacts, while taking into consideration the administrative costs associated with regulation. Moreover, Member States should consult widely on the costs and benefits of their regulatory initiatives, in particular where these imply trade-offs between different policy objectives (Integrated guideline No 9).

Guideline. To create a more attractive business environment *and to encourage private initiatives*, Member States should improve the quality of their regulations through a systematic and rigorous assessment of their economic, social and environmental impacts, while taking into consideration the administrative costs associated with regulation. Moreover, Member States should consult widely on the costs and benefits in terms of growth and employment of their regulatory *and legislative* initiatives, in particular where these imply trade-offs between different policy objectives (Integrated guideline No 9).

Modification 10

Section B, Chapter B.1, paragraph 16

Guideline. To promote a more entrepreneurial culture and create a supportive environment for SMEs, Member States should improve access to finance, adapt tax systems, strengthen the innovative potential of SMEs, and provide relevant information and support services in order to encourage the creation and growth of start-ups in line with the SMEs charter. In addition, Member States should reinforce *entrepreneurship* education and training (cross reference to the relevant employment guideline). Member States should also facilitate the transfer of ownership, revise their bankruptcy laws, and improve their rescue and restructuring proceedings (Integrated guideline No 10).

Guideline. To promote a more entrepreneurial culture and create a supportive environment for SMEs, Member States should improve access to finance, *in particular to venture capital and microcredit, reform and adapt tax systems, stimulating investment initially by harmonising the tax basis*, strengthen the innovative potential of SMEs, and provide relevant information and support services in order to encourage the creation and growth of start-ups in line with the SMEs charter. In addition, Member States should reinforce education and training *in entrepreneurship* (cross reference to the relevant employment guideline) *and in assuming risks and take measures to tackle the stigmatisation of young entrepreneurs who have not been wholly successful and help them to start again*. Member States should also facilitate the transfer of ownership, revise their bankruptcy laws, and improve their rescue and restructuring proceedings, *while improving the rules on corporate governance and managerial responsibility* (Integrated guideline No 10).

Commission recommendation

Modifications by Parliament

Modification 11

Section B, Chapter B.2, paragraph 4

Guideline. To increase and improve investment in R & D, Member States should further develop the mix of measures to foster business R & D through: improved framework conditions and ensuring that companies operate in a sufficiently competitive environment; increased and more effective public expenditure on R & D; strengthening centres of excellence; making better use of support mechanisms, such as fiscal measures to leverage private R & D; ensuring a sufficient supply of qualified researchers by attracting more students into scientific, technical and engineering disciplines and enhancing the career development and the transnational and intersectoral mobility of researchers (Integrated guideline No 12). See also integrated guideline 'Expand and improve investment in human capital' (No 22).

Guideline. To increase and improve investment in R & D, Member States should further develop the mix of measures to foster business R & D through: improved framework conditions and ensuring that companies operate in a sufficiently competitive environment; increased and more effective public expenditure on R & D; ***developing public-private partnerships***; strengthening centres of excellence; making better use of support mechanisms, such as fiscal measures to leverage private R & D; ensuring a sufficient supply of qualified researchers by attracting more students into scientific, technical and engineering disciplines and enhancing the career development and the transnational and intersectoral mobility of researchers, ***especially those European researchers who have left Europe; strengthening the link between science, research and innovation; ensuring secure public funding that strengthens centres of excellence; and increasing competition and emulation in the field of research. Member States should make greater efforts to promote the sciences of the future, such as the information society, preventive healthcare and biotechnology, in particular by promoting more objective information on the advantages and risks involved in the more controversial areas of research, such as GMO and embryo stem cell research.*** (Integrated guideline No 12). See also integrated guideline 'Expand and improve investment in human capital' (No 22).

Modification 12

Section B, Chapter B.2, paragraph 7

Guideline. To facilitate innovation and the uptake of ICT, Member States should focus on improvements in innovation support services, in particular for technology transfer, the creation of innovation poles and networks bringing together universities and enterprises, the encouragement of knowledge transfer through FDI, better access to finance and affordable and clearly defined intellectual property rights. They should facilitate the uptake of ICT and related changes in the organisation of work in the economy (Integrated guideline No 13).

Guideline. To facilitate innovation and the uptake of ICT, Member States should focus on improvements in innovation support services, in particular for technology transfer, the creation of innovation poles and networks bringing together universities and enterprises ***by facilitating the creation of incubators***, the encouragement of knowledge transfer through FDI, better access to finance and affordable and clearly defined intellectual property rights. They should facilitate the uptake of ICT and related changes in the organisation of work in the economy (Integrated guideline No 13).

Commission recommendation

Modifications by Parliament

Modification 13

Section B, Chapter B.2, paragraph 9

Guideline. To encourage the sustainable use of resources and strengthen the synergies between environmental protection and growth, Member States should give priority to the internalisation of external environmental costs; to increasing energy efficiency and to the development and application of environment-friendly technologies. The implementation of these priorities should be in line with existing European commitments and with the actions and instruments proposed in the Environmental Technologies Action Plan (ETAP), through the use of market-based instruments, risk funds and R & D funding, greening of public procurement and the removal of environmentally harmful subsidies alongside other policy instruments (Integrated guideline No 14).

Guideline. To encourage the sustainable use of resources and strengthen the synergies between environmental protection and growth, Member States should give priority to the internalisation of external environmental costs *particularly in the fields of energy, transport and agriculture* to increasing energy efficiency and to the development and application of environment-friendly technologies. *Member States should, moreover, use environmental policies more pro-actively to enhance growth and employment by developing eco-technology and eco-innovation, especially investments needed to meet the Kyoto Protocol targets, including the efficient use of traditional forms of energy, especially those which do not pose a risk to the objectives of the Kyoto Protocol;* the implementation of these priorities should be in line with existing European commitments and with the actions and instruments proposed in the Environmental Technologies Action Plan (ETAP), through the use of market-based instruments, risk funds and R & D funding, greening of public procurement and the removal of environmentally harmful subsidies alongside other policy instruments (Integrated guideline No 14).

Modification 14

Section B, Chapter B.2, paragraph 11

Guideline. To contribute to a strong European industrial base, Member States should focus on the development of new technologies and markets. This implies, in particular, commitment to the setting up and implementation of joint European technology initiatives and public-private partnerships that help tackle genuine market failures, as well as the creation and development of regional or local clusters (Integrated guideline No 15).

Guideline. To contribute to a strong European industrial base, Member States should focus on the development of new technologies and markets, *including outside Europe, to ensure that globalisation is not a threat but a new opportunity for the world's leading exporter. They should draw up a communication strategy to tackle the sense of insecurity felt by citizens in the face of globalisation, the opening up of markets and competition.* This implies, in particular, commitment to the setting up and implementation of joint European technology initiatives and public-private partnerships that help tackle genuine market failures, as well as the creation and development of regional or local clusters (Integrated guideline No 15).

12. Instructs its president to forward this resolution to the Council and Commission, and the governments and parliaments of the Member States.

4. Council recommendation of 12 July 2005 on the broad guidelines of the economic policies of the Member States and the Community (for the 2005–08 period)

THE COUNCIL OF THE EUROPEAN UNION,

Having regard to the Treaty establishing the European Community, and in particular to Article 99(2) thereof,

Having regard to the recommendation from the Commission,

Having regard to the discussion by the European Council on 16 and 17 June 2005,

Whereas a resolution on the recommendation from the Commission was adopted by the European Parliament,

HEREBY RECOMMENDS:

Introduction

The European Council of March 2005 **relaunched the Lisbon strategy by refocusing on growth and employment in Europe** ⁽¹⁾. By taking this decision, the Heads of State or Government have delivered a clear message concerning the Union's priorities over the next few years. Europe must focus its policies further on growth and employment to achieve the Lisbon goals, against a sound macroeconomic policy background and within a framework aimed at social cohesion and environmental sustainability, which are vital pillars of the Lisbon strategy.

Particular attention needs to be paid to the delivery of the Lisbon agenda. In order to achieve these objectives, the Union must do more to mobilise all the resources at national and Community levels so that their synergies can be put to more effective use. Furthermore, the involvement of relevant stakeholders can help to raise awareness of the need for growth and stability-orientated macroeconomic policies and for structural reforms, improve the quality of implementation, and increase the sense of ownership of the Lisbon strategy.

To this end, these broad economic policy guidelines (BEPGs) reflect the new start for the Lisbon strategy and concentrate on the contribution of economic policies to higher growth and more jobs. Section A of these BEPGs deals with the contribution that macroeconomic policies can make in this respect. Section B focuses on the measures and policies that the Member States should carry out in order to boost knowledge and innovation for growth and to make Europe a more attractive place to invest and work. In line with the conclusions of the Brussels European Council (22 and 23 March 2005), as a general instrument for coordinating economic policies, the BEPGs should continue to embrace the whole range of macroeconomic and microeconomic policies, as well as employment policy insofar as this interacts with those

policies; the BEPGs will ensure general economic consistency between the three strands of the strategy. The existing multilateral surveillance arrangements for the BEPGs will continue to apply.

These guidelines are applicable to all Member States and to the Community. They should foster coherence of reform measures included in the national reform programmes established by Member States and will be complemented by the Lisbon Community Programme 2005–08 covering all action to be undertaken at Community level in the interest of growth and employment. Implementation of all relevant aspects of these guidelines should take into account gender mainstreaming.

The state of the EU economy

Economic activity in the EU which had gathered momentum since mid-2003, decelerated in the second half of 2004 because of the effect of external factors such as high and volatile oil prices, the slowdown in world trade expansion and the appreciation of the euro. In part, lack of resilience in some European economies may also originate from persisting structural weaknesses. Real GDP growth is expected to continue at a moderate pace in 2005, but the lower than expected carryover from 2004 will inevitably affect the overall annual average. The contribution of domestic demand to the recovery has so far been uneven among Member States, but a gradual strengthening is expected during the year, supported by favourable financing conditions (including low real interest rates) and contained inflationary pressures.

The economic recovery has, to a large extent, been dependent upon the resurgence of global growth and the rapid increase in world trade. As the world growth cycle reaches maturity and absorbs the dampening effect of higher world oil prices, the emphasis will fall increasingly on domestic demand in the EU to provide greater impetus to the upswing. Structural and macro-policies need to be thought of against the background of an

⁽¹⁾ Conclusions of the European Council of March 2005, (http://ue.eu.int/cms3_fo/showPage.asp?lang=en&id=432&mode=g&name).

increase in the prices of raw materials, notably oil, and a downward pressure on industrial prices. The return to potential growth rates in the EU therefore depends, to a large extent, on increasing confidence among businesses and consumers, as well as on favourable global economic developments, including oil prices and exchange rates. Against this background, it is important that economic policies inspire confidence and thereby help to create conditions for stronger domestic demand and job creation in the short term, and that structural reforms contribute to an expansion of growth potential in the medium term.

Unemployment rates are projected to decrease, albeit slowly, to 8.7 % in 2006. The estimated overall employment rate is 63.0 % for EU-25 in 2003, which is significantly below the agreed target level of 70 %. Progress towards the female employment rate target of 60 % has been slow, with the rate now standing at 55.1 % for EU-25, but is expected to pick up again. The employment rate of older workers, which continued to climb to just over 40.2 % has the largest gap to bridge towards the 50 % target for 2010. At the same time, progress in improving quality in work has been mixed and the economic slowdown has raised the profile of social inclusion problems. Long-term unemployment increased

again after several years of decline and seems unlikely to fall in the near future.

The sluggishness of the EU's economic recovery is a continuing source of concern. The EU economy is in several respects further away from its goal of becoming the world's most competitive economy than was the case in March 2000. Against this background, the gulf between Europe's growth potential and that of its economic partners has not significantly narrowed.

- The first explanation for the continued under-performance of the Union economy is that its **labour input remains comparatively low**. Efforts made by the Member States allowed the employment rate to increase from 61.9 % in 1999 to 63.0 % in 2003. However, there remains a considerable scope for further improvement, notably among young and older workers, if the Lisbon targets are to be reached.
- The second key explanation for the EU's poor performance is linked to its **low level of productivity growth**. Productivity growth has been on a declining trend for several decades.

Section A. Macroeconomic policies for growth and jobs ⁽¹⁾

A.1. Macroeconomic policies creating the conditions for more growth and jobs

Securing economic stability to raise employment and growth potential

Sound macroeconomic policies are essential to support a well-balanced economic expansion and the full realisation of current growth potential. They are also vital for establishing framework conditions that will promote adequate levels of savings and investment, as well as a stronger orientation of the latter towards knowledge and innovation, so as to position the economy on a sustained, higher, non-inflationary, growth and employment path. This should help to maintain favourable long-term interest rates and to contribute to reasonable exchange rate developments. In planning for the future, firms and individuals must have confidence that price stability will be maintained.

Monetary policies can contribute by pursuing price stability and, without prejudice to this objective, by supporting other general economic policies with regard to growth and employment. For new Member States, it will be important that monetary policies contribute towards achieving sustainable real — and nominal — convergence. Exchange-rate regimes constitute an important part of the overall economic and monetary policy framework and should be orientated towards achieving real and sustainable nominal convergence. Participation in ERM II, at an appropriate stage after accession, should help those endeavours. An additional macroeconomic policy challenge for some of these Member States is to

keep current account deficits within the range where sound external financing can be secured. In this respect, fiscal restraint will be essential to reduce current account deficits.

Securing a sound budgetary position will allow the full and symmetric play of the automatic budgetary stabilisers over the cycle with a view to stabilising output around a higher and sustainable growth trend. For those

Guideline No 1. To secure economic stability for sustainable growth, 1. in line with the Stability and Growth Pact, Member States should respect their medium-term budgetary objectives. As long as this objective has not yet been achieved, they should take all the necessary corrective measures to achieve it. Member States should avoid pro-cyclical fiscal policies. Furthermore, it is necessary that those Member States having an excessive deficit take effective action in order to ensure a prompt correction of excessive deficits. 2. Member States posting current account deficits that risk being unsustainable should work towards correcting them by implementing structural reforms, boosting external competitiveness and, where appropriate, contributing to their correction via fiscal policies. See also integrated guideline ‘To contribute to a dynamic and well-functioning EMU’ (No 6).

⁽¹⁾ In implementing the policy guidelines set out below, Member States should note that the country-specific recommendations issued in the context of the Council recommendation of 26 June 2003 on the broad guidelines of the economic policies of the Member States and the Community (for the 2003–05 period) as completed and updated in the context of the Council recommendation of 5 July 2004 on the 2004 update of these guidelines, remain valid as background references.

Member States that have already achieved sound budgetary positions, the challenge is to retain that position. For the remaining Member States, it is vital to take all the necessary corrective measures to achieve their medium-term budgetary objectives, in particular if economic conditions improve, thus avoiding pro-cyclical policies and putting themselves in a position in which sufficient room for the full play of automatic stabilisers over the cycle is ensured prior to the next economic downturn. In line with the Ecofin report 'Improving the implementation of the Stability and Growth Pact' endorsed by the European Council (22 and 23 March 2005), for individual Member States the medium-term budgetary objective should be differentiated according to the diversity of economic and budgetary positions and developments as well as of fiscal risk to the sustainability of public finances, also in the face of prospective demographic changes. The Stability and Growth Pact requirements applying to the euro-area Member States also apply to ERM II Member States.

Safeguard long-term economic sustainability in the light of Europe's ageing population

Europe's ageing population poses serious risks to the long-term sustainability of the European Union economy. According to the latest projections, by 2050 the EU's population of working age (15–64) will be 18 % lower than in 2000 and the number of people aged over 65 years will have increased by 60 %. This not only implies higher dependency ratios, it also means that,

unless action is taken now to safeguard long-term fiscal sustainability, there could be an increased debt burden, due to the increase in the age-related public expenditure, and lower potential output per capita, due to the reduction in the working-age population, and future difficulties financing the pension, social insurance and health-care systems.

Member States should address the economic implications of ageing by, as part of the well-established three-pronged strategy for tackling the budgetary implications of ageing, pursuing a satisfactory pace of debt reduction and providing incentives to raise employment rates and increase labour supply so as to offset the impact of future declines in the number of persons of working age. Notwithstanding the recent increase, to 63.0 % in 2003, the still relatively low employment rate indicates that Europe has a reservoir of unused labour. The scope for further improvements is thus considerable, notably amongst women, young and older workers. In line with this strategy, it is also essential to modernise social protection systems so as to ensure that they are financially viable, providing incentives to the working-age population to actively participate in the labour market, while at the same time ensuring that they fulfil their goals in terms of access and adequacy. In particular, improved interaction between social protection systems and labour markets can remove distortions and encourage the extension of working lives against a background of increased life expectancy.

Guideline No 2. To safeguard economic and fiscal sustainability as a basis for increased employment,

Member States should, in view of the projected costs of ageing populations, 1. undertake a satisfactory pace of government debt reduction to strengthen public finances, 2. reform and re-enforce pension, social insurance and healthcare systems to ensure that they are financially viable, socially adequate and accessible, and 3. take measures to increase labour market participation and labour supply especially amongst women, young and older workers, and promote a lifecycle approach to work in order to increase hours worked in the economy. See also integrated guideline 'Promote a lifecycle approach to work' (No 18, and Nos 4, 19, 21).

Guideline No 3. To promote a growth- and employment-orientated and efficient allocation of resources

Member States should, without prejudice to guidelines on economic stability and sustainability, re-direct the composition of public expenditure towards growth-enhancing categories in line with the Lisbon strategy, adapt tax structures to strengthen growth potential, ensure that mechanisms are in place to assess the relationship between public spending and the achievement of policy objectives and ensure the overall coherence of reform packages. See also integrated guideline 'To encourage the sustainable use of resources and strengthen the synergies between environmental protection and growth' (No 11).

Promote a growth, employment-orientated and efficient allocation of resources

Well-designed tax and expenditure systems that promote an efficient allocation of resources are a necessity for the public sector to make a full contribution towards growth and employment, without jeopardising the goals of economic stability and sustainability. This can be achieved by redirecting expenditure towards growth-enhancing categories such as research and development (R & D), physical infrastructure, environmentally friendly technologies, human capital and knowledge. Member States can also help to control other expenditure categories through the use of expenditure rules and performance budgeting and by putting assessment mechanisms in place to ensure that individual reform measures and overall reform packages are well designed. A key priority for the EU economy is to ensure that tax structures and their interaction with benefit systems promote higher growth potential through more employment and investment.

Guideline No 4. To ensure that wage developments contribute to macroeconomic stability and growth and to increase adaptability, Member States should encourage the right framework conditions for wage-bargaining systems, while fully respecting the role of the social partners, with a view to promoting nominal wage and labour-cost developments consistent with price stability and the trend in productivity over the medium term, taking into account differences across skills and local labour market conditions. See also integrated guideline ‘Ensure employment-friendly labour-cost developments and wage-setting mechanisms’ (No 22).

Ensure that wage developments contribute to growth and stability and complement structural reforms

Wage developments can contribute to stable macroeconomic conditions and an employment-friendly policy mix provided that real wage increases are in line with the underlying rate of productivity growth over the medium term and are consistent with a rate of profitability that allows for productivity, capacity and employment-enhancing investment. This requires that temporary factors such as variation in productivity caused by cyclical factors or one-off rises in the headline rate of inflation do

not cause an unsustainable trend in wage growth and that wage developments reflect local labour market conditions.

Given the continued upward pressure on oil and raw material prices, vigilance is needed over the impact of wage settlements and labour-cost increases on price stability and price competitiveness. The fact that this second-round effect has not been observed so far is welcome. These issues need to be taken into account in the continued dialogue and information exchange between monetary and fiscal authorities and the social partners via the macroeconomic dialogue.

Promote coherent macroeconomic, structural and employment policies

The role of sound macroeconomic policies is to provide conditions conducive to employment creation and growth. Structural reforms, consistent with sound fiscal positions in the short and medium term, are essential to increase productivity and employment in the medium term, thus leading to the full realisation and strengthening of growth potential. They also contribute to fiscal sustainability, macroeconomic stability and resilience to shocks. At the same time, appropriate macroeconomic policies are key towards reaping the full benefits of

Guideline No 5. To promote greater coherence between macroeconomic, structural and employment policies, Member States should pursue labour and product market reforms that, at the same time, increase the growth potential and support the macroeconomic framework by increasing flexibility, factor mobility and adjustment capacity in labour and product markets in response to globalisation, technological advances, demand shift, and cyclical changes. In particular, Member States should renew impetus in tax and benefit reforms to improve incentives and to make work pay; increase adaptability of labour markets combining employment flexibility and security; and improve employability by investing in human capital. See also integrated guideline ‘Promote flexibility combined with employment security and reduce labour market segmentation, having due regard to the role of the social partners’ (No 21, and No 19).

structural reforms in term of growth and employment. A key feature of Member States' overall economic strategy is to ensure that they have a consistent set of structural policies that support the macroeconomic framework and vice versa. In particular, market reforms need to improve the overall adaptability and adjustment capacity of economies in response to changes in cyclical economic conditions and also longer-term trends such as globalisation and technology. In this regard, an effort towards reforms of tax and benefit systems should be pursued in order to make work pay and avoid any possible disincentive for labour market participation.

A.2. Ensuring a dynamic and well-functioning euro area

The need to achieve higher growth and employment is particularly acute in the euro area given its recent subdued economic performance and its low level of potential growth of around 2 % (Commission estimates). In its last spring forecast, the Commission revised downwards its prevision for 2005 at a 1.6 % growth in the eurozone. Economic divergence may increase in the euro zone, in terms of growth, internal demand and inflation pressures. The deceleration of economic growth in the euro area in the second half of last year can be attributed to both external factors — high and volatile oil prices, slowing global trade growth and the appreciation of the euro — as well as internal rigidities. On the external side, adverse oil price developments and persisting global imbalances continue to represent non-negligible downside risks.

Domestic demand has been particularly muted in the euro area, with both private consumption and investment significantly below that of the EU-25 as a whole in 2004. Muted private consumption seems to be rooted in continuing concerns regarding, in particular, employment prospects (with unemployment continuing to be around 9 %) as well as income prospects in the medium term. The level of confidence and the lack of sustained improvement on the consumption side have continued to weigh on investment.

The challenge for the euro area is to ensure the realisation of current growth potential and even more to raise its growth potential over time. This is best achieved through growth and stability orientated macroeconomic policies and comprehensive structural reforms. Both are also particularly salient for euro-area and ERMII Mem-

ber States as they have an important impact on their capacity to adequately adjust to shocks with an asymmetric impact and therefore on the economic resilience of the euro area as a whole. Furthermore, the economic performance of, and policies pursued by, individual euro-area Member States affect common goods such as the euro's exchange rate, interest rates price stability and the cohesion of the euro area. All this implies a need for effective policy coordination, both in the EU and in the euro area, to improve growth potential and performance.

The absence of national interest and exchange-rate policies implies also an increased need to achieve and maintain sound budget positions over the cycle which provide a sufficient budgetary margin to absorb the impact of cyclical fluctuations or economic shocks with an asymmetric impact. Structural policies that foster the smooth adjustment of prices and wages are essential to ensure that euro-area Member States have the capacity to rapidly adjust to shocks (such as the current oil price shock) and to help to avoid unwarranted inflationary developments. Policies that increase the responsiveness of labour markets, through encouraging widespread labour participation, occupational and geographical mobility and the setting of wages, together with appropriate product-market reforms, are particularly important in this respect.

In the short run, the policy mix in the euro area needs to support economic recovery while, at the same time, safeguarding long-term sustainability and stability. At the current juncture, it is important that the policy mix underpins confidence among consumers and investors which also implies remaining committed to medium-term stability. Budgetary policy has to ensure a fiscal position consistent with the need to prepare for the impact of ageing populations on the one hand and to accomplish a composition of public expenditure and revenues that fosters economic growth on the other.

To contribute to international economic stability and better represent its economic interests, it is critical for the euro area to play its full role in international monetary and economic policy cooperation. Whilst a stable Eurogroup Presidency will help to coordinate euro-area members' positions, the external representation of the euro area has to be improved, on the basis of the framework of the Vienna agreement of 11 and 12 December 1998, so that the euro area can take a leading strategic role in the development of the global economic system.

Guideline No 6. To contribute to a dynamic and well-functioning EMU, euro-area Member States need to ensure better coordination of their economic and budgetary policies, in particular 1. pay particular attention to fiscal sustainability of their public finances in full compliance with the Stability and Growth Pact; 2. contribute to a policy mix that supports economic recovery and is compatible with price stability, and thereby enhances confidence among business and consumers in the short run, while being compatible with long-term sustainable growth; 3. press forward with structural reforms that will increase euro-area long-term potential growth and will improve its productivity, competitiveness and economic adjustment to asymmetric shocks, paying particular attention to employment policies; and 4. ensure that the euro area's influence in the global economic system is commensurate with its economic weight.

Section B. Microeconomic reforms to raise Europe's growth potential

Structural reforms are essential to increase the EU's growth potential and support macroeconomic stability, because they increase the efficiency and adaptability of the European economy. Productivity gains are fuelled by competition, investment and innovation. Raising Europe's growth potential requires making progress in both job creation and productivity growth. Since the mid-1990s, productivity growth in the EU has slowed down markedly. Part of this slowdown comes from increased employment of low-skilled workers. However, reversing this trend in productivity is a major challenge facing the Union, especially in the light of its ageing population. Population ageing alone is estimated to reduce by nearly half the current rate of potential growth. An acceleration of productivity growth and increasing hours worked are thus indispensable to maintain and increase future living standards, and ensure a high level of social protection.

B.1. Knowledge and innovation — engines of sustainable growth

Knowledge accumulated through investment in R & D, innovation and education is a key driver of long-run growth. Policies aimed at increasing investment in knowledge and strengthening the innovation capacity of the EU economy are at the heart of the Lisbon strategy for growth and employment. This is why national and regional programmes will be increasingly targeted on investments in these fields in accordance with the Lisbon objectives.

Increase and improve investment in R & D, with a view to establishing the European knowledge area

R & D affects economic growth through various channels: first, it can contribute to the creation of new markets or production processes; second, it can lead to incremental improvements in already existing products and

production processes; and third, it increases the capacity of a country to absorb new technologies.

The EU is currently spending around 2 % of GDP on R & D (although ranging from below 0.5 % to above 4 % of GDP across Member States), barely up from the level at the time of the launch of the Lisbon strategy. Moreover, only around 55 % of research spending in the EU is financed by the business sector. Low levels of private R & D investments are identified as one of the main explanations for the EU/US innovation gap. More rapid progress towards meeting the collective EU target of raising research investment to 3 % of GDP is needed. Member States are invited to report on their R & D expenditure targets for 2008 and 2010 and the measures to achieve these in their national Lisbon programmes. The main challenge is to put in place framework conditions, instruments and incentives for companies to invest in research.

Public research expenditure must be made more effective and the links between public research and the private sector have to be improved. Poles and networks of excellence should be strengthened, better overall use should be made of public-support mechanisms to boost private-sector innovation, and a better leverage effect of public investments and a modernised management of research institutions and universities should be ensured. It is also essential to ensure that companies operate in a competitive environment since competition provides an important incentive to private spending on innovation. In addition, a determined effort must be made to increase the number and quality of researchers active in Europe, in particular by attracting more students into scientific, technical and engineering disciplines, and enhancing the career development and the transnational and intersectoral mobility of researchers, and reducing barriers to mobility of researchers and students.

The international dimension of R & D should be strengthened in terms of joint financing, development of a more critical mass at EU level in critical areas requiring large funds and through reducing barriers to mobility of researchers and students.

Guideline No 7. To increase and improve investment in R & D, in particular by private business, the overall objective for 2010 of 3 % of GDP is confirmed with an adequate split between private and public investment, Member States will define specific intermediate levels. Member States should further develop a mix of measures appropriate to foster R & D, in particular business R & D, through: 1. improved framework conditions and ensuring that companies operate in a sufficiently competitive and attractive environment; 2. more effective and efficient public expenditure on R & D and developing PPPs; 3. developing and strengthening centres of excellence of educational and research institutions in Member States, as well as creating new ones where appropriate, and improving the cooperation and transfer of technologies between public research institute and private enterprises; 4. developing and making better use of incentives to leverage private R & D; 5. modernising the management of research institutions and universities; 6. ensuring a sufficient supply of qualified researchers by attracting more students into scientific, technical and engineering disciplines and enhancing the career development and the European, international as well as inter-sectoral mobility of researchers and development personnel.

Facilitate innovation

The dynamism of the European economy is crucially dependent on its innovative capacity. The economic framework conditions for innovation need to be in place. This implies well-functioning financial and product markets as well as efficient and affordable means to enforce intellectual property rights. Innovations are often introduced to the market by new enterprises, which may meet particular difficulties in obtaining finance.

Measures to encourage the creation and growth of innovative enterprises, including improving access to finance, should therefore enhance innovative activity. Technology diffusion, and policies to better integrate national innovation and education systems, can be fostered by the development of innovation poles and networks as well as by innovation support services targeted at SMEs. Knowledge transfer via researcher mobility, foreign direct investment (FDI) or imported technology is particularly beneficial for lagging countries and regions.

Guideline No 8. To facilitate all forms of innovation, Member States should focus on: 1. improvements in innovation support services, in particular for dissemination and technology transfer; 2. the creation and development of innovation poles, networks and incubators bringing together universities, research institutions and enterprises, including at regional and local level, helping to bridge the technology gap between regions; 3. the encouragement of cross-border knowledge transfer, including from foreign direct investment; 4. encouraging public procurement of innovative products and services; 5. better access to domestic and international finance, and 6. efficient and affordable means to enforce intellectual property rights.

The diffusion of information and communication technologies (ICT), in line with the objectives and actions of the upcoming i2010 initiative, is also an important way to improve productivity and, consequently, economic growth. The EU has been unable to reap the full benefits of the increased production and use of information and communication technologies (ICT). This reflects the still continuing under-investment in ICT, institutional constraints and organisational challenges to the adoption of ICT. Technological innovation ultimately depends on a growth-conducive economic environment. In this context, the use of intelligent logistics is an efficient way of ensuring that costs at the European sites of production remain competitive. A market of electronic communication, open and competitive, is also important in this regard.

Guideline No 9. To facilitate the spread and effective use of ICT and build a fully inclusive information society, Member States should:

1. encourage the widespread use of ICT in public services, SMEs and households; 2. fix the necessary framework for the related changes in the organisation of work in the economy; 3. promote a strong European industrial presence in the key segments of ICT; 4. encourage the development of strong ICT and content industries, and well-functioning markets; 5. ensure the security of networks and information, as well as convergence and interoperability in order to establish an information area without frontiers; 6. encourage the deployment of broad-band networks, including for the poorly served regions, in order to develop the knowledge economy. See also integrated guideline 'Promote flexibility combined with employment security and reduce labour market segmentation, having due regard to the role of the social partners' (No 21).

To strengthen the competitive advantages of the European industrial base

The recent slowdown in EU productivity growth is partly related to the EU's difficulty in re-orienting its economy towards the higher productivity growth sectors.

In order to enhance and sustain economic and technological leadership, Europe must increase its capacity to develop and market new technologies, including ICT. The synergies from jointly addressing research, regulatory and financing challenges at European level, where for reasons of scale or scope, individual Member States cannot successfully tackle market failures in isolation, should be analysed and exploited. The EU has still not managed to fully realise its technological potential. The pooling of European excellence and the development of public-private partnerships and cooperation between Member States where the benefits for society are larger than those for the private sector will help tap this potential.

Encourage the sustainable use of resources

Lasting success for the Union also depends on addressing a range of resource and environmental challenges which, if left unchecked, will act as a brake on future

Guideline No 10. To strengthen the competitive advantages of its industrial base, Europe needs

a solid industrial fabric throughout its territory. The necessary pursuit of a modern and active industrial policy means strengthening the competitive advantages of the industrial base, including by contributing to attractive framework conditions for both manufacturing and services, while ensuring the complementarity of the action at national, transnational and European levels. Member States should: 1. start by identifying the added value and competitiveness factors in key industrial sectors, and addressing the challenges of globalisation. 2. also focus on the development of new technologies and markets. (a) This implies, in particular, commitment to promote new technological initiatives based on public-private partnerships and cooperation between Member States, that help tackle genuine market failures. (b) This also implies the creation and development of networks of regional or local clusters across the EU with greater involvement of SMEs. See also integrated guideline 'Improve matching of labour market needs' (No 20).

growth. In this context, recent developments and prospects on oil prices have emphasised the acuity of the energy efficiency issue. A policy towards energy efficiency is important to reduce the vulnerability of the European economy to oil price variations. Further delay in addressing these challenges would raise the economic costs of taking action. This implies, for example, measures to make more rational use of resources. Measures in this area will also be important to tackle the problem of climate change. In this context, it is important that Member States renew efforts to meet the obligations according to the Kyoto Protocol. Member States should notably continue the fight against climate change in order to achieve that the global temperature increase does not exceed 2 °C above pre-industrial levels, while implementing the Kyoto targets in a cost-effective way. Member States should pursue the engagement of halting the loss of biological diversity between now and 2010, in particular by incorporating this requirement into other policies, given the importance of biodiversity for certain economic sectors. The use of market-based instruments, so that prices better reflect environmental damage and

social costs, plays a key role in this context. Encouraging the development and use of environment-friendly technologies, the greening of public procurement, paying particular attention to SMEs, and the removal of environmentally harmful subsidies alongside other policy instruments can improve the innovative performance and enhance the contribution to sustainable development of the sectors concerned. For example, EU companies are amongst the world leaders in developing new renewable energy technologies. In particular, in a context of continued upward pressure on energy prices, and accumulating threats to the climate, it is important to push energy efficiency improvements as a contribution to both growth and sustainable development.

B.2 Making Europe a more attractive place to invest and work

The attractiveness of the European Union as an investment location depends *inter alia* on the size and openness of its markets, its regulatory environment, the quality of its labour force and its infrastructure.

Extend and deepen the internal market

Whilst the internal market for goods is relatively well integrated, services markets remain, legally or *de facto*, rather fragmented and labour mobility remains low in Europe. In order to promote growth and employment and to strengthen competitiveness, the internal market of services has to be fully operational while preserving the European social model. The European Council has requested all efforts to be undertaken within the legislative process in order to secure a broad consensus for moving towards a single market for services. The elimination of obstacles to cross-border activities would also bring important efficiency gains. Finally, the full integration of financial markets would raise output and employment by allowing more efficient allocation of capital and creating better conditions for business finance.

Despite general acknowledgement of the potential benefits of a single European market, the transposition rate of internal market directives remains disappointingly low. Furthermore, directives are often not implemented or applied correctly, as illustrated by the high number of infringement proceedings launched by the Commission. Member States need to cooperate more positively with each other and with the Commission to ensure that they deliver the full benefits of internal market legislation to their citizens and businesses. For example, there is considerable scope for further improvements in public pro-

Guideline No 11. To encourage the sustainable use of resources and strengthen the synergies between environmental protection and growth,

Member States should: 1. give priority to energy efficiency and co-generation, the development of sustainable, including renewable, energies and the rapid spread of environmentally friendly and eco-efficient technologies (a) inside the internal market on the one hand, particularly in transport and energy, *inter alia* in order to reduce the vulnerability of the European economy to oil price variations, (b) towards the rest of the world on the other hand as a sector with a considerable export potential; 2. promote the development of means of internalisation of external environmental costs and decoupling of economic growth from environmental degradations. The implementation of these priorities should be in line with existing Community legislation and with the actions and instruments proposed in the Environmental Technologies Action Plan (ETAP), *inter alia*, through (a) the use of market-based instruments, (b) risk funds and R & D funding, (c) the promotion of sustainable production and consumption patterns, including the greening of public procurement, (d) paying particular attention to SMEs and (e) a reform of subsidies that have considerable negative effects on the environment and are incompatible with sustainable development, with a view to eliminating them gradually. 3. pursue the objective of halting the loss of biological diversity between now and 2010, in particular by incorporating this requirement into other policies, given the importance of biodiversity for certain economic sectors. 4. continue to fight against climate change, while implementing the Kyoto targets in a cost-effective way, particularly with regard to SMEs. See also integrated guideline 'To promote a growth- and employment-orientated and efficient allocation of resources' (No 3).

urement practices. Such improvements would be reflected in an increase in the share of public procurement publicly advertised. Moreover, more open procurement would lead to significant budgetary savings for the Member States.

Guideline No 12. To extend and deepen the internal market, Member States should:

1. speed up the transposition of internal market directives; 2. give priority to stricter and better enforcement of internal market legislation; 3. eliminate remaining obstacles to cross-border activity; 4. apply EU public procurement rules effectively; 5. promote a fully operational internal market of services, while preserving the European social model; 6. accelerate financial market integration by a consistent and coherent implementation and enforcement of the Financial Services Action Plan. See also integrated guideline 'To improve matching of labour market needs' (No 20)

Ensure open and competitive markets inside and outside Europe

The open global economy offers new opportunities for stimulating growth and competitiveness in Europe's economy. Competition policy has played a key role in ensuring a level playing field for firms in the EU, and can also be instrumental to look at the wider regulatory framework around markets, in order to promote the conditions which will allow firms to compete effectively. A further opening up of European markets to competition can be achieved by a reduction in the general level of remaining State aid. This movement must be accompanied by a redeployment of remaining State aid in favour of support for certain horizontal objectives. The review of State aid rules should lead to a further push in this direction.

Structural reforms that ease market entry are a particularly effective tool for enhancing competition. These will be particularly important in markets that were previously sheltered from competition because of anti-competitive behaviour, the existence of monopolies, over-regulation (for example permits, licences, minimum capital requirements, legal barriers, shop opening hours, regulated prices, etc. may hinder the development of an effective competitive environment), or because of trade protection.

In addition, the implementation of measures already agreed to open up the network industries to competition (in the areas of electricity and gas, transport, telecommu-

nications and postal services) should help to ensure lower prices overall and greater choice while guaranteeing the delivery of services of general economic interest to all citizens. Competition and regulatory authorities should ensure competition in liberalised markets. At the same time, the satisfactory delivery of high-quality services of general economic interest at an affordable price must be guaranteed.

External openness to trade and investment, also in a multilateral context, by increasing both exports and imports, is an important spur to growth and employment and can thus reinforce the delivery of structural reform. An open and strong system of global trade rules is of vital importance for the European economy. The successful completion of an ambitious and balanced agreement in the framework of the Doha Round as well as the development of bilateral and regional free trade agreements, should further open up markets to trade and investment, thus contributing to raising potential growth.

Guideline No 13. To ensure open and competitive markets inside and outside Europe and to reap the benefits of globalisation, Member States should give priority to:

1. the removal of regulatory, trade and other barriers that unduly hinder competition; 2. a more effective enforcement of competition policy; 3. selective screening of markets and regulations by competition and regulatory authorities in order to identify and remove obstacles to competition and market entry; 4. a reduction in State aid that distorts competition; 5. in line with the upcoming Community framework, a redeployment of aid in favour of support for certain horizontal objectives such as research, innovation and the optimisation of human capital and for well-identified market failures; 6. the promotion of external openness, also in a multilateral context; 7. full implementation of the agreed measures to open up the network industries to competition in order to ensure effective competition in European-wide integrated markets. At the same time, the delivery, at affordable prices, of effective services of general economic interest has an important role to play in a competitive and dynamic economy.

Improve European and national regulation

Market regulation is essential to creating an environment in which commercial transactions can take place at competitive prices. It also serves to correct market failures or to protect market participants. Nevertheless, the cumulative impact of regulations may impose substantial economic costs. It is therefore essential that regulations are well designed and proportionate. The quality of the European and national regulatory environments is a matter of joint commitment and shared responsibility at both EU and Member State levels.

When preparing or revising legislation, Member States should systematically assess the costs and benefits of their legislative initiatives. They should improve the quality of their regulations, while preserving their objectives. This implies consultation of relevant stakeholders. In the Commission's approach to better regulation, the economic, social and environmental impacts of new or revised regulations are carefully assessed to identify the potential trade-offs and synergies between different policy objectives. Moreover, existing regulation is screened for simplification potential and its impact on competitiveness is assessed. Finally, a common approach to measuring the administrative costs of new and existing legislation is being developed. Member States should establish systems for simplification of existing regulation. They should consult widely on the costs and benefits of their regulatory initiatives or their lack of action, particularly where trade-offs between different policy objectives are implied. Member States should also ensure that appropriate alternatives to regulation are given full consideration.

Significant improvements in the regulatory environment can therefore be achieved by taking into account cost-benefit considerations associated with regulation, including administrative costs. This is especially important for small and medium-sized enterprises (SMEs), which usually have only limited resources to deal with the administration imposed by both Community and national legislation.

Europe needs to foster its entrepreneurial drive more effectively and it needs more new firms willing to embark on creative or innovative ventures. Learning about entrepreneurship through all forms of education and training should be supported and relevant skills provided. The entrepreneurship dimension should be integrated in the life-long learning process as from school. To this end, partnerships with companies should be

***Guideline No 14. To create a more competitive business environment and encourage private initiative through better regulation,** Member States should: 1. reduce the administrative burden that bears upon enterprises, particularly on SMEs and start-ups; 2. improve the quality of existing and new regulations, while preserving their objectives, through a systematic and rigorous assessment of their economic, social (including health) and environmental impacts, while considering and making progress in measurement of the administrative burden associated with regulation, as well as the impact on competitiveness, including in relation to enforcement; 3. encourage enterprises in developing their corporate social responsibility.*

encouraged. The creation and growth of businesses can also be encouraged by improving access to finance and strengthening economic incentives, including by adopting tax systems to reward success, reducing non-wage labour costs and reducing the administrative burdens for start-up notably through the provision of relevant business support services, notably for young entrepreneurs, like the creation of one-stop contact points and the stimulation of national support networks for enterprises. Particular emphasis should be put on facilitating the transfer of ownership and improving rescue and restructuring proceedings in particular with more efficient bankruptcy laws.

Expand and improve European infrastructure

Modern infrastructure is an important factor affecting the attractiveness of locations. It facilitates the mobility of persons, goods and services throughout the Union. Modern transport, energy and electronic communication infrastructure is an important factor of a re-invigorated Lisbon strategy. By reducing transport costs and by widening markets, interconnected and interoperable trans-European networks help foster international trade and fuel internal market dynamics. Moreover, the ongoing liberalisation of European network industries fosters competition and drives efficiency gains in these sectors.

In terms of future investment in European infrastructure, the implementation of 30 priority transport projects identified by Parliament and Council in the trans Euro-

Guideline No 15. To promote a more entrepreneurial culture and create a supportive environment for SMEs, Member States should:

1. improve access to finance, in order to favour their creation and growth, in particular micro-loans and other forms of risk capital; 2. strengthen economic incentives, including by simplifying tax systems and reducing non-wage labour costs; 3. strengthen the innovative potential of SMEs, and 4. provide relevant support services, like the creation of one-stop contact points and the stimulation of national support networks for enterprises, in order to favour their creation and growth in line with small firms' charter. In addition, Member States should reinforce entrepreneurship education and training for SMEs. They should also facilitate the transfer of ownership, modernise where necessary their bankruptcy laws, and improve their rescue and restructuring proceedings. See also integrated guidelines 'To promote a growth- and employment-orientated and efficient allocation of resources' (No 3) and 'To facilitate all forms of innovation' (No 8), Nos 23 and 24.

pean network (TEN) transport guidelines as well as the implementation of the quick-start cross-border projects for transport, renewable energy and broadband communications and research identified under the European initiative for growth and the implementation of the transport projects supported by the Cohesion Fund should be

considered a priority. Infrastructure bottlenecks within countries need to be tackled as well. Appropriate infrastructure pricing systems can contribute to the efficient use of infrastructure and the development of a sustainable modal balance.

Guideline No 16. To expand, improve and link up European infrastructure and complete priority cross-border projects with the particular

aim of achieving a greater integration of national markets within the enlarged EU. Member States should: 1. develop adequate conditions for resource-efficient transport, energy and ICT infrastructures — in priority, those included in the TEN networks — by complementing Community mechanisms, notably including in cross-border sections and peripheral regions, as an essential condition to achieve a successful opening up of the network industries to competition; 2. consider the development of public-private partnerships; 3. consider the case for appropriate infrastructure pricing systems to ensure the efficient use of infrastructures and the development of a sustainable modal balance, emphasising technology shift and innovation and taking due account of environmental costs and the impact on growth. See also integrated guideline 'To facilitate the spread and effective use of ICT and build a fully inclusive information society' (No 9).

List of contents of *European Economy*

Basic editions

1, November 1978

- Annual Economic Report 1978–79
- Annual Economic Review 1978–79

2, March 1979

- European monetary system
— Texts of the European Council of 4 and 5 December 1978

3, July 1979

- Short-term economic trends and prospects
- The European monetary system
— Commentary
— Documents

4, November 1979

- Annual Economic Report 1979–80
- Annual Economic Review 1979–80

5, March 1980

- Short-term economic trends and prospects
- Adaptation of working time

6, July 1980

- Short-term economic trends and prospects — Borrowing and lending instruments looked at in the context of the Community's financial instruments

7, November 1980

- Annual Economic Report 1980–81
- Annual Economic Review 1980–81

8, March 1981

- Economic trends and prospects — The Community's borrowing and lending operations recent developments

9, July 1981

- Fifth medium-term economic policy programme — The main medium-term issues: an analysis

10, November 1981

- Annual Economic Report 1981–82
- Annual Economic Review 1981–82

11, March 1982

- Economic trends and prospects — Unit labour costs in manufacturing industry and in the whole economy

12, July 1982

- Documents relating to the European monetary system

13, September 1982

- The borrowing and lending activities of the Community in 1981

14, November 1982

- Annual Economic Report 1982–83
- Annual Economic Review 1982–83

15, March 1983

- Economic trends and prospects — Budgetary systems and procedures — Industrial labour costs — Greek capital markets

16, July 1983

- Business investment and the tax and financial environment — Energy and the economy: a study of the main relationships in the countries of the European Community — The foreign trade of the Community, the United States and Japan

17, September 1983

- The borrowing and lending activities of the Community in 1982

18, November 1983

- Annual Economic Report 1983–84
- Annual Economic Review 1983–84

19, March 1984

- Economic trends and prospects — Industrial labour costs — Medium-term budget balance and the public debt — The issue of protectionism

20, July 1984

- Some aspects of industrial productive performance in the European Community: an appraisal — Profitability, relative factor prices and capital/labour substitution in the Community, the United States and Japan, 1960–83 — Convergence and coordination of macroeconomic policies: some basic issues

21, September 1984

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