Translation

ASSEMBLY OF THE PORTUGUESE REPUBLIC

EUROPEAN AFFAIRS COMMITTEE

Opinion

COM (2014) 423

COUNCIL RECOMMENDATION on Portugal’s 2014 national reform programme and delivering a Council opinion on Portugal’s 2014 stability programme

PART I - INTRODUCTION

Pursuant to Article 7 of Law No 43/2006 of 25 August 2006 on the monitoring, examination and issuing of opinions by the Assembly of the Portuguese Republic in the context of the process of EU integration, as amended by Law No 21/2012 of 17 May 2012, and in accordance with the Guidelines for the Scrutiny of EU Initiatives approved on 8 January 2013, the European Affairs Committee received the COUNCIL RECOMMENDATION on Portugal’s 2014 national reform programme and delivering a Council opinion on Portugal’s 2014 stability programme [COM(2014)423].

In view of its subject-matter, the initiative was forwarded to the Committee on Budgetary and Financial Affairs and Public Administration, which analysed it and approved the Report annexed to this Opinion, of which it is an integral part.

PART II - GROUNDS

This initiative is based on the working document of the Commission1. It examines Portugal's 2014 national reform programme and its 2014 stability programme and formulates a set of recommendations for the period 2014-2015.

It should be recalled that as a result of the international crisis that badly affected Portugal, in particular from 2009, the country was subject to a macroeconomic adjustment programme from May 2011 to June 2014. During this period Portugal was exempt from the monitoring and assessment of the European Semester for economic policy coordination, and thereby from the obligation to submit a national reform programme and a stability programme.

Nevertheless, in April 2014, Portugal submitted a fiscal strategy document and a letter providing an update on developments on the Europe 2020 strategy. In May 2014, the Portuguese Government also presented its ongoing reform programme and new initiatives towards sustainable growth in a document entitled 'The Road to Growth, a medium-term reform strategy for Portugal'.

[1] SWD(2014) 423.

As Portugal has officially exited the macroeconomic adjustment programme, it has now been reinstated in the European Semester framework.

Against this background, the European Commission has assessed the documents submitted by the Portuguese Government, resulting in a set of recommendations set out in the initiative currently under examination.

In the light of the provisions of the proposal, the following must be considered:

a) Legal basis

The legal basis of this initiative is Article 121(2) and Article 148(4) of the Treaty on the Functioning of the European Union (TFEU).[2]

b) Content of the initiative

The document alludes to the success of the Portuguese macroeconomic adjustment programme, emphasising that 'significant fiscal consolidation' has been achieved. It also applauds the fact that 'Portugal's economic recovery is firming' and that the unemployment rate has fallen.

However, despite a positive overall assessment, the European Commission stresses that 'significant challenges remain in the area of budgetary, financial and structural policies'.

The initiative therefore lists a series of risks which, according to the Commission, should not be overlooked, in the following areas in particular:

i) <u>Fiscal policy</u> - In this area, it is deemed that implementation and legal risks remain 'as various consolidation measures have been challenged on constitutional grounds'. It is therefore recommended that there be 'sustained further consolidation after the correction of the excessive deficit to achieve the medium-term objective of a structural deficit of 0.5% of GDP by 2017.' Public debt, which 'is expected to stabilise at around 130.5% of GDP in 2014',

[2] Consolidated versions of the Treaty on European Union and the Treaty on the Functioning of the European Union.

should then start falling gradually. To achieve this, measures should be taken to bring public debt on a decreasing downward path towards the 60% of GDP threshold.

ii) Fiscal-structural reforms - It is deemed that 'tight expenditure restraint must be maintained at all levels of government'. 'The accumulation of public-sector arrears' should 'be stopped, including by ensuring full financial sustainability of state-owned enterprises. On the revenue side, there is still scope for making the tax-system more growth-friendly and further strengthening tax compliance'.

iii) Financial sector - While considering that financial stability has been preserved, there are elements that pose challenges to bank stability, such as high non-performing-loans ratios and elevated corporate-debt levels.

iv) Labour market - It is stressed that 'Portugal faces challenges relating to unemployment which, notwithstanding the recent decline, remains very high, particularly for the younger cohorts. The unemployment rate stood at 17% in 2013 and youth unemployment at 37.7%, substantially above the EU average, as well as the percentage of young people not in education, employment, or training.' Moreover, improvements in the collective bargaining system are necessary to 'make wages more flexible and responsive to economic conditions.' The document states that nominal unit labour costs increased by 1.1% in 2013, thanks to the reinstatement of the 13th and 14th month salaries in the public sector. However, 'unit labour costs are estimated to have fallen by more than 6% between 2009 and 2014, contributing importantly to the improvement in Portugal's external competitiveness.' Therefore, 'unit labour costs will have to fall further'. The Portuguese Government should also enhance the effectiveness of active labour market policies.

v) Poverty - It is pointed out that 'while the measures adopted in the context of the Programme have been designed with a view to minimising the impact on the most disadvantaged, Portugal's economic and financial crisis has had negative implications for poverty and inequality. The number of jobless households not covered by social benefits remains one of the highest in the EU'.

vi) Education - In this area, it is recommended that 'the expansion of the number of schools under autonomy agreement and the measures put in place to increase the attractiveness and quality of vocational training' be monitored effectively. A recent Communication from the European Commission entitled 'Taking stock of the Europe 2020 strategy for smart, sustainable and inclusive growth' notes that with regard to the targets set in the area of early leaving from education 'most of the Member States are likely to meet their target, with the exception of Spain, Portugal and Romania.' As regards the rate of tertiary education completion, it is stressed that more efforts need to be made in countries like Portugal, Malta and Slovakia 'that are far from reaching these targets'.

vii) Growth-enhancing structural reforms - It is recognised that a more innovation-friendly business environment is needed to introduce more dynamism into the economy. Although Portugal has expanded its research and innovation system over the last decade, it is still 'underperforming compared with the EU average. There is a lack of cooperation between public research and the business sector, and knowledge transfer and knowledge commercialisation are very weak.' It is therefore recommended that the Portuguese Government set clear priorities in this area, in order to promote the development of competitive economic activities. In the transport sector, there is a need 'to implement the comprehensive long-term transport plan, to integrate ports into the overall logistics and transport system and to strengthen competition in the railway and metropolitan transport sectors'. In the energy sector, the focus is on the need to tackle excess revenues so as to reduce energy costs, thereby encouraging economic growth.

In summary, the document under examination recommends that Portugal implement a set of measures within the period 2014-2015, to:

i) 'Rigorously implement the budgetary strategy as laid out in the Fiscal Strategy Document 2014, in order to bring the deficit to 2.5% of GDP';

ii) 'Replace consolidation measures which the Constitutional Court considers unconstitutional by measures of similar size and quality as soon as possible [...] pursue the planned annual structural adjustment towards the medium-term objective, in line with the requirement of an annual structural adjustment of at least 0.5% of GDP, more in good times, and ensure that the debt rule is met in order to put the high general debt ratio on a sustainable path';

iii) 'Develop a durable solution to ensure the medium-term sustainability of the pensions system by the end of 2014';

iv) 'Control health care expenditure growth and proceed with the hospital reform';

v) 'Effectively implement single wage and supplements' scales in the public sector from 2015 onwards';

vi) 'Maintain minimum wage developments consistent with the objectives of promoting employment and competitiveness. Ensure a wage-setting system that promotes the alignment of wages and productivity at sectoral and/or firm level';

vii) 'Ensure efficient public expenditure in education and reduce skills mismatches' on the labour market;

viii) 'Monitor banks' liquidity position and potential capital shortfalls, including by on-site thematic inspections and stress-testing';

ix) Set up, by the end of September 2014, 'an early warning system to detect weak financial conditions of firms, including SMEs, with a view to supporting early corporate debt restructuring';

x) 'Eliminate payment delays by the public sector';

xi) 'Ensure adequate resources of the national regulators and competition authority and swiftly adopt the by-laws of the national competition authority';

xii) 'Continue to rationalise and modernise central, regional and local public administration. Implement the reforms to enhance the efficiency of the judicial system and increase transparency'.

PART III - OPINION OF THE RAPPORTEUR

Our analysis of the initiative and of the accompanying documents shows that at both national and European level, completion of the macroeconomic adjustment programme was not nearly as successful as announced. To substantiate this claim, one has only to look at a few indicators, for instance: **public debt**, which stood at 94% of GDP at the end of 2010, is expected to reach **130.9% of GDP** at the end of **2014**; the **unemployment rate**, which stood at 10.8% at the end of 2010, is expected to reach **14.2% in 2014**; the **population at risk of poverty or social exclusion**, which stood at 25.3% at the end of 2010, is expected to rise to **27.4%** by the end of **2014**. This is the harsh reality of numbers, and numbers are not influenced by ideology.

The documents examined show that not only was Europe unprepared to deal with a crisis of such magnitude but that it was also unable to make up for this lack of preparedness effectively, causing millions of Europeans to be buffeted by the crisis, even jeopardising European solidarity and cohesion.

The political choices made proved to be inadequate. At national level the Portuguese Government, always striving to be a 'good pupil in the European class', wished not only to live up to its reputation but to exceed it. So it went full steam ahead and implemented the measures, but the Portuguese economy, in particular SMEs, micro-businesses and most of all Portuguese citizens in general, ended up paying a heavy price. At the end of the three-year financial assistance programme, it has to be recognised that, unlike what a member of the party in office proclaimed, neither the country nor Portuguese citizens are in better shape. On the contrary, Portugal and its citizens have become poorer, and social inequalities have widened.

The set of recommendations which the EU is asking Portugal to implement in 2014-2015, and which has been diligently accepted by the Government, is clearly an example of continuing to bark up the wrong tree, the wrong tree being fiscal consolidation measures based primarily on reducing public expenditure by lowering wages and cutting spending on health, education, social benefits and pensions. Admittedly, Portugal has experienced a rise in exports over the past few years, but this is not enough to turn the country around over the next decade. Indeed, the European Union itself recently stated that exports will not continue to drive economic growth as in the period from 2010 to 2012.

It is obvious that the only way out of the vicious circle of the crisis is to make a firm commitment to economic growth and to adopt new patterns that promote research and science in order to foster sustainable development, which in turn will create wealth and new and better jobs.

The debate on fiscal flexibility should be encouraged, following the line taken by Mario Draghi in his recent speech at the Jackson Hole symposium.

If nothing is done and the EU continues to steer the same course, there will be a very high social and political price to pay.

PART IV - OPINION

In the light of the information set out above and the report of the relevant committee, the European Affairs Committee's opinion is as follows:

1. There is no need to assess the compliance of this initiative with the subsidiarity principle, as it is a non-legislative initiative.

2. This concludes the scrutiny of this initiative. However, given the political significance of the issues involved, the European Affairs Committee will continue to monitor the process, including the exchange of information with the Government.

Palácio de São Bento, 23 September 2014

The Rapporteur	**The Chairman of the Committee**
[*Signature*]	[*Signature*]
(Ivo Oliveira)	**(Paulo Mota Pinto)**

PART V – ATTACHMENT

Report of the Committee on Budgetary and Financial Affairs and Public Administration.

ASSEMBLY OF THE PORTUGUESE REPUBLIC

Committee on Budgetary and Financial Affairs and Public Administration

Report

Council Recommendation

COM(2014)423

on Portugal's 2014 national reform programme and delivering a Council opinion on Portugal's 2014 stability programme.

Rapporteur: Member Lídia Bulcão

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Pursuant to Article 7(1), (2) and (3) of Law No 43/2006 of 25 August 2006 (as amended by Law No 21/2012 of 17 May 2012) on the monitoring, examination and issuing of opinions by the Assembly of the Portuguese Republic in the context of the process of EU integration, the Council Recommendation on Portugal's 2014 national reform programme and delivering a Council opinion on Portugal's 2014 stability programme [COM(2014)423] was sent, together with the Assessment of the 2014 national reform programme and stability programme for Portugal [SWD(2014)423], on 4 June 2014 to the Committee on Budgetary and Financial Affairs and Public Administration so that it could be analysed and this report drawn up, in line with the Committee's remit.

PART II - GROUNDS

1. General points

• Purpose of the initiative

This initiative is a Council recommendation following completion of Portugal's macroeconomic adjustment programme. During this period Portugal was exempt from submitting a stability programme and a national reform programme, pursuant to Regulation (EU) No 472/2013.

After Portugal submitted an updated fiscal strategy document on 30 April 2014 and a letter from the Portuguese Government containing a progress report on compliance with the objectives of the Europe 2020 strategy, and given that at the end of the macroeconomic adjustment programme Portugal will be fully reinstated in the European Semester, the European Commission assessed the above documents taking into consideration not only their relevance for a sustainable budgetary and socio-economic policy in Portugal but also their compliance with the EU's rules and guidelines, given the need to strengthen the EU's overall economic governance by providing EU input for future national decisions.

This assessment resulted in a comprehensive Commission Staff Working Document, which accompanies the initiative under examination and served as a basis for the recommendations made by the Council in this initiative.

2. Relevant issues

• Analysis of and opinion on substantive issues relating to the initiative

In the light of the Commission's assessment, the Council examined Portugal's stability programme. Its opinion is reflected in a set of recommendations prepared following the successful conclusion of the economic adjustment programme and aimed at securing the lasting implementation of the programme's achievements.

Similarly, based on a prior analysis of economic policy in the euro area as a whole, conducted by the Commission in the context of the European Semester, the Council also recommends that Portugal implement the specific recommendations made by the Council to Member States whose currency is the euro.

• Possible implications for Portugal

The Commission's recommendations for Portugal under the European Semester are reflected in a set of eight points set out in the initiative, in which the Council recommends that Portugal take action within the period 2014-2015 to:

1) fully implement the budgetary strategy for 2014 and replace consolidation measures which the Constitutional Court considers unconstitutional by measures of similar size and quality as soon as possible, prioritising expenditure-based fiscal consolidation, increasing further the efficiency and quality of public expenditure and ensuring strict compliance with the Law on Commitments and Late Payments;

2) maintain minimum wage developments consistent with the objectives of promoting employment and competitiveness;

3) present, by March 2015, an independent evaluation of the recent reforms in the employment protection system, together with an action plan for possible further reforms to tackle labour market segmentation and youth unemployment;

4) improve the quality and labour-market relevance of the education system in order to reduce early school leaving and address low educational performance rates, ensure efficient public expenditure in education and reduce skills mismatches, and enhance cooperation between public research and business;

5) monitor banks' liquidity position and potential capital shortfalls, implement a comprehensive strategy to reduce the corporate debt overhang and reinforce efforts to widen the range of financing alternatives, and ensure that the identified measures support the reallocation of financing towards the productive sectors of the economy;

6) implement the second and third package of measures in the energy sector aimed at reducing energy costs for the economy, and eliminate the electricity tariff debt by 2020;

7) further improve the evaluation of the Portuguese housing market, including by setting up, by the end of November 2014, a more systematic monitoring and reporting framework and issue a comprehensive report on the shadow economy in that market;

8) continue to rationalise and modernise central, regional and local public administration, implement the reforms to enhance the efficiency of the judicial system and increase transparency, insert mandatory systematic assessments in the legislation process, and set up a functionally independent central evaluation unit at government level, which assesses and reports every six months on the implementation of these reforms.

3. Principle of subsidiarity

As this is a non-legislative initiative, there is no need to examine compliance with the principle of subsidiarity.

PART III - OPINION OF THE RAPPORTEUR

The Rapporteur reserves the right not to express an opinion on the initiative in this forum.

PART IV - CONCLUSIONS

In view of the above, the Committee on Budgetary and Financial Affairs and Public Administration concludes that:

1. There is no need to assess the compliance of this initiative with the subsidiarity principle, as it is a non-legislative initiative.

2. Given the content of this initiative, whose recommendations will have a significant impact on Portugal's future, it is proposed that the development and implementation of the recommendations listed be monitored by the Assembly of the Republic and the Committee on Budgetary and Financial Affairs and Public Administration.

3. The Committee on Budgetary and Financial Affairs and Public Administration considers its examination of this initiative to be complete. Pursuant to Law No 43/2006 of 25 August 2006, this Opinion must be forwarded to the European Affairs Committee for the appropriate purposes.

Palácio de São Bento, 9 July 2014,

The Rapporteur
[*Signature*]
(Lídia Bulcão)

The Chairman of the Committee
[*Signature*]
(Eduardo Cabrita)