

A PACT FOR THE EURO

STRONGER ECONOMIC POLICY COORDINATION FOR COMPETITIVENESS AND CONVERGENCE

Euro area Heads of State and Government have decided to adopt a Pact for the Euro to strengthen the economic pillar of the monetary union, achieve a new quality of economic policy coordination in the Euro area, improve competitiveness, thereby leading to a higher degree of convergence. This Pact focuses primarily on areas that fall under national competence and are key for increasing competitiveness and avoiding harmful imbalances. Competitiveness is essential to help the EU grow faster and more sustainably in the medium and long term, to produce higher levels of income for citizens, and to preserve our social models. Non-euro area Member States are invited to participate on a voluntary basis.

This renewed effort for stronger economic policy coordination for competitiveness and convergence rests on **four guiding rules**:

- a. It will be *in line with and strengthen the existing economic governance* in the EU, while providing added value. It will be consistent with and build on existing instruments (EU 2020, European Semester, Integrated Guidelines, Stability and Growth Pact and new macro-economic surveillance framework). It will involve a special effort going beyond what already exists and include concrete commitments and actions that are more ambitious than those already agreed, and accompanied with a timetable for implementation. These new commitments will thereafter be included in the National Reform and Stability Programmes and be subject to the regular surveillance framework, with a strong central role for the Commission in the monitoring of the implementation of the commitments, and the involvement of all the relevant formations of the Council and the Eurogroup. The European Parliament will play its full role in line with its competences. Social partners will be fully involved at the EU level through the Tripartite Social Summit.
- b. It will be focused, action oriented, and cover *priority policy areas that are essential for fostering competitiveness and convergence*. It will concentrate on actions where the competence lies with the Member States. In the chosen policy areas *common objectives will be agreed upon at the Heads of State or Government level. Participating Member States will pursue these objectives with their own policy-mix, taking into account their specific challenges*.
- c. *Each year, concrete national commitments will be undertaken by each Head of State or Government*. In doing so, Member States will take into account best practices and benchmark against the best performers, within Europe and vis-à-vis other strategic partners.

The implementation of commitments and progress towards the common policy objectives will be *monitored politically by the Heads of State or Government* of the Euro area and participating countries on a yearly basis, on the basis of a report by the Commission. In addition, Member States commit to consult their partners on each major economic reform having potential spill-over effects before its adoption.

- d. Euro area Member States are fully committed to the completion of the Single Market which is key to enhancing the competitiveness in the EU and the Euro area. This process will be fully in line with the treaty. *The Pact will fully respect the integrity of the Single Market*.

Our goals

Euro area Member States undertake to take all necessary measures to pursue the following objectives:

- Foster competitiveness
- Foster employment
- Contribute further to the sustainability of public finances
- Reinforce financial stability

Each participating Member State will present the specific measures it will take to reach these goals. If a Member State can show that action is not needed on one or the other areas, it will not include it. The choice of the specific policy actions necessary to achieve the common objectives *remains the responsibility of each country, but particular attention will be paid to the set of possible measures mentioned below.*

Concrete policy commitments and monitoring

Progress towards the common objectives above will be politically monitored by the Heads of State or Government on the basis of a series of indicators covering competitiveness, employment, fiscal sustainability and financial stability. Countries facing major challenges in any of these areas will be identified and will have to commit to addressing these challenges in a given timeframe.

a. Foster competitiveness

Progress will be assessed on the basis of wage and productivity developments and competitiveness adjustment needs. To assess whether wages are evolving in line with productivity, unit labour costs (ULC) will be monitored over a period of time, by comparing with developments in other Euro area countries and in the main comparable trading partners. For each country, ULCs will be assessed for the economy as a whole and for each major sector (manufacturing; services; as well as tradable and non-tradable sectors). Large and sustained increases may lead to the erosion of competitiveness, especially if combined with a widening current account deficit and declining market shares for exports. Action to raise competitiveness is required in both all countries, but particular attention will be paid to those facing major challenges in this respect. To ensure that growth is balanced and widespread in the whole Euro area, specific instruments and common initiatives will be envisaged to foster productivity in regions lagging behind.

Each country will be responsible for the specific policy actions it chooses to foster competitiveness, but the following reforms will be given particular attention:

- (i) respecting national traditions of social dialogue and industrial relations, measures to ensure costs developments in line with productivity, such as:
 - review the wage setting arrangements, and, where necessary, the degree of centralisation in the bargaining process, and the indexation mechanisms, while maintaining the autonomy of the social partners in the collective bargaining process;

- ensure that wages settlements in the public sector support the competitiveness efforts in the private sector (bearing in mind the important signalling effect of public sector wages).

(ii) measures to increase productivity, such as:

- further opening of sheltered sectors by measures taken at the national level to remove unjustified restrictions on professional services and the retail sector, to foster competition and efficiency, in full respect of the Community *acquis*;
- specific efforts to improve education systems and promote R&D, innovation and infrastructure;
- measures to improve the business environment, particularly for SMEs, notably by removing red tape and improving the regulatory framework (e.g. bankruptcy laws, commercial code).

b. Foster employment

A well functioning labour market is key for the competitiveness of the Euro area. Progress will be assessed on the basis of the following indicators: long term and youth unemployment rates, and labour participation rates.

Each country will be responsible for the specific policy actions it chooses to foster employment, but the following reforms will be given particular attention:

- labour market reforms to promote “flexicurity”, reduce undeclared work and increase labour participation;
- life long learning;
- tax reforms, such as lowering taxes on labour to make work pay while preserving overall tax revenues, and taking measures to facilitate the participation of second earners in the work force.

c. Enhance the sustainability of public finances

In order to secure the full implementation of the Stability and Growth Pact, the highest attention will be paid to:

▪ Sustainability of pensions, health care and social benefits

This will be assessed notably on the basis of the sustainability gap indicators¹. These indicators measure whether debt levels are sustainable based on current policies, notably pensions schemes, health care and benefit systems, and taking into account demographic factors.

¹ The sustainability gap are indicators agreed by the Commission and Member States to assess fiscal sustainability.

Reforms necessary to ensure the sustainability and adequacy of pensions and social benefits could include:

- aligning the pension system to the national demographic situation, for example by aligning the effective retirement age with life expectancy or by increasing participation rates;
- limiting early retirement schemes and using targeted incentives to employ older workers (notably in the age tranche above 55).

▪ National fiscal rules

Euro area Member States commit to translating EU fiscal rules as set out in the Stability and Growth Pact into national legislation. Member States will retain the choice of the specific national legal vehicle to be used, but will make sure that it has a sufficiently strong binding and durable nature (e.g. constitution or framework law). The exact formulation of the rule will also be decided by each country (e.g. it could take the form of a "debt brake", rule related to the primary balance or an expenditure rule), but it should ensure fiscal discipline at both national and sub-national levels. The Commission will have the opportunity, in full respect of the prerogatives of national parliaments, to be consulted on the precise fiscal rule before its adoption so as to ensure it is compatible with, and supportive of, the EU rules.

d. Reinforce financial stability

A strong financial sector is key for the overall stability of the Euro area. A comprehensive reform of the EU framework for financial sector supervision and regulation has been launched.

In this context, Member States commit to putting in place national legislation for banking resolution, in full respect of the Community *acquis*. Strict bank stress tests, coordinated at EU level, will be undertaken on a regular basis. In addition, the President of the ESRB and the President of the Eurogroup will be invited to regularly inform Heads of State or Government on issues related to macro-financial stability and macroeconomic developments in the Euro area requiring specific action. In particular, for each Member State, the level of private debt for banks, households and non-financial firms will be closely monitored.

In addition to the issues mentioned above, attention will be paid to **tax policy coordination**.

Direct taxation remains a national competence. Pragmatic coordination of tax policies is a necessary element of a stronger economic policy coordination in the Euro area to support fiscal consolidation and economic growth. In this context, Member States commit to engage in structured discussions on tax policy issues, notably to ensure the exchange of best practices, avoidance of harmful practices and proposals to fight against fraud and tax evasion.

Developing a common corporate tax base could be a revenue neutral way forward to ensure consistency among national tax systems while respecting national tax strategies, and to contribute to fiscal sustainability and the competitiveness of European businesses.

The Commission intends to present a legislative proposal on a common consolidated corporate tax base in the coming weeks.

Concrete yearly commitments

In order to demonstrate a real commitment for change and ensure the necessary political impetus to reach our common objectives, each year Member States of the Euro area will agree at the highest level on a set of concrete actions to be achieved within 12 months. The selection of the specific policy measures to be implemented will remain the responsibility of each country, but the choice will be guided by considering in particular the issues mentioned above. These commitments will also be reflected in the National Reform Programmes and Stability Programmes submitted each year which will be assessed by the Commission, the Council, and the Eurogroup in the context of the European Semester.

Next steps

The Pact will be formally adopted at the EC on 24 March by Euro area Member States and those Member States non participating in the euro which wish so. Those MS in a position to do so should announce already on 24 March the concrete commitments to be achieved in the next 12 months. In any event, concrete commitments should be included in the National Reform and Stability Programmes to be submitted in April and will be presented to the June European Council.
