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From:	Presidency
To:	Delegations
Subject:	Conclusions of the Ministerial Dialogue between the Economic and Finance Ministers of teh EU and the Candidate Countries of 9 July 2013

Delegations will find attached the Conclusions of the Ministerial Dialogue between the Economic and Finance Ministers of the EU and the Candidate Countries of 9 July 2013.

ANNEX

CONCLUSIONS OF THE MINISTERIAL DIALOGUE BETWEEN THE ECONOMIC AND FINANCE MINISTERS OF THE EU AND THE CANDIDATE COUNTRIES

The Economics and Finance Ministers of the EU and the candidate countries, representatives of the Commission and the European Central Bank and representatives of the central banks of the candidate countries met for their 15th economic policy dialogue. Ministers welcomed the submission of the 2013 Pre-accession Economic Programmes (PEP) of Iceland, the former Yugoslav Republic of Macedonia, Montenegro, Serbia and Turkey which outline the countries' medium-term macroeconomic frameworks, fiscal strategies and structural reform agendas. The programmes cover the period from 2013-2015.

Conclusions

Ministers acknowledge that candidate countries have overall managed to safeguard macroeconomic stability in difficult circumstances. However, ensuring a transparent analysis of the structural bottlenecks to growth and candidate countries' strong commitment to execute further important measures are essential for achieving sustainable economic growth and stability. In this light, Ministers underline the existence of potential sources of downside risks and vulnerabilities and therefore call for further determined action and invite the candidate countries to implement the required sustainable growth-oriented policy measures and structural reforms.

As regards Iceland, Ministers welcomed the remarkable efforts made at stabilising the economy after the near collapse of Icelandic financial system but important risks remain. The existing capital restrictions are limiting competition in capital markets, have a negative impact on the business climate and risk deterring domestic and foreign investment. Ministers therefore invite Iceland to further develop its strategy for a gradual liberalisation of capital flows complemented by macro-prudential tools to safe-guard macro-financial stability.

Ministers acknowledge that headline inflation moderated in the course of 2012, but still remained above the upper threshold of the inflation target. In this respect, Ministers underlined the continued need for a rather tight monetary policy stance and commended the central bank's vigilance in this respect.

Ministers underline the existence of structural bottlenecks, such as the country's low degree of economic diversification, which make the country vulnerable to asymmetric shocks and impede the lifting of its growth potential. In order to close existing productivity gaps, it seems essential to further open up the economy to international competitive forces and to increase firms' economies of scale. Moreover, Ministers invite Iceland to increase potential growth by increasing efficiency gains in sectors suffering from low labour productivity.

Ministers note that a high level of public debt of around 100% of GDP remains a source of vulnerability and welcome the authorities' intention to reduce the debt ratio to 60% of GDP through continued fiscal consolidation. In this context, Ministers stressed that the recent recourse to ad-hoc and temporary measures to enhance revenues may improve the fiscal position in the short term, but does not spare the authorities from developing and enacting a set of structural fiscal policy measures that could effectively support fiscal policy objectives in the medium-to-long term. Along with this, the composition of the budget would need to be changed towards more growth-conducive spending and revenue patterns.

Ministers also encourage Iceland to further enhance the information included in the PEP, by (i) providing alternative growth scenarios and analysing in more detail the links between the financial sector and the medium-term growth scenario (ii) detailing the measures envisaged to further reinforce the financial sector supervision (iii) discussing more in-depth the sustainability and financing of the current account deficit and (iv) providing a clear timeline and sequencing of the planned reform measures along with information about their estimated budgetary impact.

As regards the former Yugoslav Republic of Macedonia, Ministers welcome the envisaged reform priorities in the area of the labour market, education and the business environment that would address structural weaknesses and raise the country's growth potential. Furthermore, Ministers encourage the country to implement further measures to increase competitiveness, i.e. through enhancing innovation and further diversifying exports towards higher-value markets, thereby also reducing structural unemployment.

Ministers welcome efforts of the central bank to tightly manage the exchange rate, which thus far served the country well by anchoring the inflation expectations, which in turn allowed monetary authorities to pursue a mix of standard and non-standard measures in order to support economic growth. However, Ministers underline that restoration of the bank lending channel and lingering concerns on banks' asset quality will remain challenging and should be addressed.

In view of the moderate but rising debt and deficit levels, Ministers encourage the authorities to put in place a credible plan to return to a sustainable fiscal path. Ministers stress in this regard that the fiscal framework still lacks consistency, and therefore invite the authorities to continue strengthening their fiscal planning and administrative capacities.

Finally, Ministers encourage the former Yugoslav Republic of Macedonia to resume the submission of fiscal notifications and ensure compliance with the ESA 95 classification. Ministers furthermore stress that the PEP would benefit from spelling out the concrete measures implementing fiscal and structural reform strategies, including their timeline and expected impacts.

As regards Montenegro, Ministers welcome the planned reforms that are targeted to tackle the country's structural weaknesses. They also stress that additional efforts are required to further stabilize the still fragile banking sector and invite the authorities to improve the situation by strengthening the banking regulation and supervisory framework and addressing challenges related to banks' asset quality.

Ministers note that external imbalances remain a structural issue and that the economy is exposed to significant financing requirements to cover the current account deficit as well as the amortization of external debt.

In the context of unilateral euroisation[1], the scope for monetary policy in Montenegro is very limited, which enhances the role of fiscal policy and structural reforms, Ministers note that the high general government deficit and the rising public debt call for further fiscal adjustments and consolidation.

In the long-run, creating a competitive environment will mainly have to rely on the continuation of structural reforms with a view to raise labour and capital productivity. Ministers in this regard stress the importance of sufficiently diversifying the economic activities, fighting against high youth and long-term unemployment and reducing exposure to exogenous risks like energy and commodity price shocks.

Ministers encourage Montenegro to strengthen fiscal and financial stability as a prerequisite for long-term economic growth and to enhance the PEP by further elaborating on the analysis of external sustainability, sources of growth and competitiveness.

[1] Ministers recall the Council position on unilateral euroisation from 2007 which should be fully taken into consideration by the Montenegrin authorities.

As regards Serbia, Ministers acknowledge that most of the structural weaknesses are identified by the authorities and that the measures needed to address them are either envisaged or in preparation. However, Ministers stress that the timely implementation of these measures remains a key challenge. In order to ensure the credibility to the reform agenda, Serbia needs to operationalize the various reform intentions and design clear action plans for their implementation. Accelerating structural reforms to increase the productivity and support a shift towards a more sustainable growth model is crucial for improving the medium- and long-term outlook.

In circumstances where a strong depreciation of the currency would have posed severe consequences for financial and macroeconomic stability due to the country's considerable degree of euroisation, Ministers acknowledge the efforts of the central bank to mitigate such consequences by frequent interventions in the FX market and the stepwise reduction of surplus liquidity, and welcome the gradual tightening of the monetary policy stance with a view to stabilising inflation expectations. However, Ministers underline the need to further strengthen the monetary policy framework by solidly anchoring inflation expectations, which coupled with a stable and independent central bank is a critical element of the inflation targeting regime, as well as improving the resilience of the financial and banking sector in order to improve the monetary policy transmission mechanism.

Ministers underline the need for ambitious, frontloaded and expenditure-based fiscal adjustment. Overall, Ministers stress that sustained efforts are needed to put public finances on a sound footing, including through comprehensive structural reforms to reduce and restructure public expenditure in order to ensure sustainable fiscal adjustment and create more space for growth-enhancing expenditure. In particular, Ministers underline that streamlining state aid and further reforms of the pension system are urgently needed.

Ministers stress that further measures should be taken in order to reduce the administrative and regulatory barriers in the economy. Furthermore, strengthening competition and improving the functioning of product markets would be needed to limit inflation volatility and thus reduce the burden put on monetary policy in Serbia. Ministers also acknowledge that bold measures would be required to address youth and long-term unemployment and to prompt sustainable employment creation.

Ministers encourage Serbia to enhance the information included in the PEP by (i) designing an alternative macroeconomic scenario (ii) more explicitly linking the macroeconomic scenarios with the structural reform measures.

As regards Turkey, Ministers welcome the policy measures geared towards a soft landing of the economy and the subsequent reduction in external imbalances.

Ministers also acknowledge that the mix of monetary and macro-prudential policies of the central bank has contributed to this outcome. On the other hand, as some of the implemented measures have reduced monetary policy predictability, Ministers call for more transparency in monetary policy decisions. They also draw attention to the medium term objective of price stability as inflation, although it has decelerated, remains high and inflation expectations are still elevated.

Ministers welcome the recent reform of private pensions and the fiscal discipline envisaged over the medium-term. By promoting domestic savings, they can reduce high reliance on short term external financing, a vulnerability that has been mitigated by the sharp decline of the current account deficit in 2012 but is likely to re-emerge as future growth is to be driven by domestic demand. They encourage Turkey to preserve a sufficiently restrictive fiscal stance as this would also improve the macro-economic policy mix.

Structural reforms to strengthen the investment climate would be conducive to higher private investment and lead to higher foreign direct investment, thus ensuring a more sustainable financing of the current account and improving the competitiveness of the economy. Ministers in this context call on Turkey to upgrade and better use its human capital, through the pursuit of the education agenda and the deepening and widening of labour market reforms. At the same time, they note that there is scope for a further strengthening of competition through continuing the liberalisation of product and service markets, especially in non-traded services, thereby reducing upward price pressures and boosting productivity.

Ministers encourage Turkey to enhance the information included in the PEP by identifying measures underlying the fiscal and structural reform strategies.

Overall, Ministers underline their commitment to this surveillance process which should ensure a continued anchoring of the candidate countries' medium-term economic programmes. Ministers also encourage candidate countries to make further progress with respect to their macroeconomic, budgetary and structural policies. Ministers will meet again in the course of 2014 to continue their dialogue. Likewise, the dialogue at the level of the Economic and Financial Committee and its counterparts will continue in 2014.

As regards statistics, Ministers underline the importance of reliable and contemporary data and therefore welcome the 2013 Progress Report on the Action Plan on Economic, Monetary and Financial Statistics in Candidate Countries. They were comforted that all candidate countries made progress in fulfilling the Action Plan requirements, but noted that additional efforts in some statistical areas are still needed to achieve a full compliance with the Action Plan requirements.