**COUNCIL OF
THE EUROPEAN UNION**

Brussels, 4 June 2012

10550/12

**UEM 133
ECOFIN 468
SOC 451
COMPET 345
ENV 433
EDUC 142
RECH 194
ENER 220**

COVER NOTE

from:	Secretary-General of the European Commission, signed by Mr Jordi AYET PUIGARNAU, Director
date of receipt:	1 June 2012
to:	Mr Uwe CORSEPIUS, Secretary-General of the Council of the European Union
No Cion doc.:	COM(2012) 324 final
Subject:	Recommendation for a Council Recommendation on Portugal's 2012 national reform programme and delivering a Council opinion on Portugal's stability programme for 2012-2016

Delegations will find attached Commission document COM(2012) 324 final.

Encl.: COM(2012) 324 final

EUROPEAN COMMISSION

Brussels, 30.5.2012
COM(2012) 324 final

Recommendation for a

COUNCIL RECOMMENDATION

on Portugal's 2012 national reform programme

and delivering a Council opinion on Portugal's stability programme for 2012-2016

{SWD(2012) 324 final}

Recommendation for a

COUNCIL RECOMMENDATION

on Portugal's 2012 national reform programme

and delivering a Council opinion on Portugal's stability programme for 2012-2016

THE COUNCIL OF THE EUROPEAN UNION,

Having regard to the Treaty on the Functioning of the European Union, and in particular Articles 121(2) and 148(4) thereof,

Having regard to Council Regulation (EC) No 1466/97 of 7 July 1997 on the strengthening of the surveillance of budgetary positions and the surveillance and coordination of economic policies[1], and in particular Article 5(2) thereof,

Having regard to the recommendation of the European Commission[2],

Having regard to the resolutions of the European Parliament[3],

Having regard to the conclusions of the European Council,

Having regard to the opinion of the Employment Committee,

After consulting the Economic and Financial Committee,

Whereas:

(1) On 26 March 2010, the European Council agreed to the European Commission's proposal to launch a new strategy for jobs and growth, Europe 2020, based on enhanced coordination of economic policies, which will focus on the key areas where action is needed to boost Europe's potential for sustainable growth and competitiveness.

(2) On 13 July 2010, the Council adopted a recommendation on the broad guidelines for the economic policies of the Member States and the Union (2010 to 2014) and, on 21 October 2010, adopted a decision on guidelines for the employment policies of the Member States[4], which together form the 'integrated guidelines'. Member States were

---

1 OJ L 209, 02.08.1997, p. 1
2 COM(2012)324 final
3 P7_TA(2012)0048 and P7_TA(2012)0047
4 Council Decision 2012/238/EU of 26 April 2012

invited to take the integrated guidelines into account in their national economic and employment policies.

(3) On 12 July 2011, the Council adopted a recommendation on Portugal’s national reform programme for 2011.

(4) On 23 November 2011, the Commission adopted the second Annual Growth Survey, marking the start of the second European Semester of ex-ante and integrated policy coordination, which is anchored in the Europe 2020 strategy.

(5) On 2 March 2012, the European Council endorsed the priorities for ensuring financial stability, fiscal consolidation and action to foster growth. It underscored the need to pursue differentiated, growth-friendly fiscal consolidation, to restore normal lending conditions to the economy, to promote growth and competitiveness, to tackle unemployment and the social consequences of the crisis, and to modernise public administration.

(6) On 2 March 2012, the European Council also invited the Member States participating in the Euro Plus Pact to present their commitments in time for inclusion in their stability or convergence programmes and their national reform programmes.

(7) On 2 May 2012, Portugal submitted its stability programme covering the period 2012-2016 and on 7 May 2012, Portugal submitted its national reform programme.

(8) On 17 May 2011, the Council adopted Implementing Decision 2011/344/EU to make available to Portugal medium-term financial assistance for a period of three years from 2011 to 2014 in accordance with Council Regulation (EU) No 407/2010 of 11 May 2010 establishing a European financial stabilisation mechanism. The accompanying Memorandum of Understanding signed on the same day and its successive supplements lay down the economic policy conditions on the basis of which the financial assistance is disbursed.

(9) Portugal has made good progress on a number of fronts, but significant challenges remain. Achieving the fiscal targets remains essential if the government is to regain full market access within the programme period. To limit the risks to the 2012 fiscal targets, rapid and determined implementation of the structural-fiscal measures of the programme is paramount. At the same time, the government needs to focus on reforms that address Portugal’s competitiveness challenges. The 2012 budget does not pursue earlier plans of a ‘fiscal devaluation’. This makes it all the more important to adopt rapidly additional structural reforms in the labour and product markets with a view to reducing labour costs, increasing flexibility and lowering entry barriers. Perseverance and resolve on the part of the government will be required to overcome strong vested interests that stand in the way of reforms.

(10) Overall, the Third Review of the Economic Adjustment Programme has concluded that Portugal's implementation of the conditionality set out in the Memorandum of Understanding remains on track. In particular, the fiscal deficit target for 2011 (5.9% of GDP) has been overachieved by resorting to a transfer of banks' pension funds to the state amounting to 3½ per cent of GDP. Despite this one-off operation, the structural consolidation in 2011 was large and amounted to 3½ per cent of GDP. Banks are on track to meet the capital requirements under the Programme by the end of the year but capital positions have to improve further in 2012 in line with

Programme requirements and as a result of the European Banking Authority's requirement to cater for sovereign exposures, the special on-site inspection programme and the planned transfer of banks' private pension plans.

(11) The decline of GDP in 2011 was less marked than forecast, as exports and consumption performed better than foreseen. However, the fourth quarter of 2011 and beginning of 2012 showed weak domestic demand, a sharp rise in unemployment and low business confidence. According to the Commission spring forecast, the outlook for 2012 has deteriorated and GDP is now projected to fall by 3.3 per cent, i.e. three percentage points more than in the autumn forecast. Economic growth in 2013 will also be more limited than originally expected. While the external adjustment has so far been remarkably fast, with Portuguese exports gaining market shares outside the EU and imports falling considerably, its persistence is still uncertain. Given the large external debt Portugal has accumulated, very substantial further adjustment of a structural nature is required.

(12) The budget for 2012 targets a government deficit of 4.5% of GDP, which is in line with the Economic Adjustment Programme requirements and with the Council recommendations given to Portugal under the Excessive Deficit Procedure. Medium-term fiscal consolidation plans presented in the stability programme are also consistent with the Economic Adjustment Programme's deficit headline targets and a deficit-to-GDP ratio of 3% of GDP is expected by 2013. The 2012 budget includes consolidation measures amounting to more than 5% of GDP, which are made up of permanent structural measures. Two thirds of the measures are on the expenditure side and include a significant cut of public sector wages and pensions, a reduction in the number of government employees by 2% (full-time equivalent) and a rationalisation of state-owned enterprises. On the revenue side, the budget envisages a reduction in tax exemptions, an increase in the number of goods and services taxed at the standard VAT rate, higher personal income and corporate taxes, an increase in excise taxes and enhanced efforts to fight tax evasion and fraud. The deficit is expected to decrease further to 1.8% of GDP in 2014 and 1% of GDP in 2015. The main risks to the budgetary targets are mainly related to the state-owned enterprise sector and local and regional governments. In terms of the structural balance, the fiscal structural adjustment is expected to be over 7 percentage points of GDP in 2011-2012. The MTO of -0.5% of GDP adequately reflects the requirements of the Stability and Growth Pact. As regards public debt, it is expected to peak at 115.7% of GDP in 2013 and gradually decline thereafter.

(13) The success of the Economic Adjustment Programme depends crucially on the implementation of a wide range of structural reforms that will remove the rigidities and bottlenecks that underlie the economy's decade-long stagnation. Noticeable progress has been made until now. The far-reaching and ambitious reform agenda is on track in the areas of labour market, health care, housing, judiciary and the insolvency and regulatory framework including competition. Also, privatisations so far have been highly successful. In network industries, progress was more mixed. In particular, in the energy sector a comprehensive strategy to eliminate the sector's rising debt by tackling excessive rents remains to be fleshed out.

(14) A strategic re-programming of the Structural Funds is underway, with a focus on support to youth employment and competitiveness (in particular SMEs). The new

measures strengthen actions in the areas of employment passport, training and professional qualifications and access to finance for Small and Medium Enterprises.

(15) Portugal has made a number of commitments under the Euro Plus Pact. The commitments, and the implementation of the commitments presented in 2011, relate to improving competitiveness, the employment rate and the sustainability of public finances, while strengthening financial sustainability.

HEREBY RECOMMENDS that Portugal should take action within the period 2012-2013 to:

Implement the measures as laid down in Implementing Decision 2011/344/EU and further specified in the Memorandum of Understanding of 17 May 2011 and its subsequent supplements.

Done at Brussels,

For the Council
The President