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CORRIGENDUM
This document corrects document COM(2019) 150 final of 27.2.2019.
Concerns all language versions.
Correction of footnote 7.
The text shall read as follows:

COMMUNICATION FROM THE COMMISSION TO THE EUROPEAN PARLIAMENT, THE EUROPEAN COUNCIL, THE COUNCIL, THE EUROPEAN CENTRAL BANK AND THE EUROGROUP

2019 European Semester: Assessment of progress on structural reforms, prevention and correction of macroeconomic imbalances, and results of in-depth reviews under Regulation (EU) No 1176/2011

{SWD(2019) 1000 à 1027 final}

1. INTRODUCTION

The European Union enjoys its seventh year of economic growth. **Such sustained growth has helped Europe's economy in providing jobs to a record number of people.** 240 million Europeans are currently in employment, with 15 million new jobs created since 2013. The EU unemployment rate has fallen to record lows and now stands at 6.6%.

In addition, public finances have improved, with the public debt-to-GDP ratio being back on a downward path since 2015 and the deficit estimated below 1% of GDP as of 2018. The implementation of structural reforms, investment and responsible fiscal policies in the Member States, combined with decisive action at European level, including the Investment Plan for Europe, have contributed to the renewed stability and greater prosperity enjoyed today in the European economy.

Growth in Europe has slowed down, partly due to the deterioration of the global economic environment. The EU growth rate is expected to slow down from the estimated 1.9% in 2018 to 1.5% in 2019, before picking up to 1.7% in 2020. Global trade and geopolitical tensions are on the rise, and the EU is impacted particularly, due to the geographical and sector orientation of its exports. Still, the European Union is maximising the benefits of trade. For instance, the recently concluded EU-Japan free trade agreement has the potential to increase EU's annual exports to Japan by EUR 13.5 billion. Given the uncertainty over the terms of the UK's future relations with the EU, this Communication does not speculate on the possible economic implications of different scenarios.

Growth drivers are shifting from external to domestic. Higher employment and growth is set to support private consumption, while investment should continue to benefit from favourable financing conditions. Eliminating restrictions to the functioning of the Single Market and the improvement of the business environment should continue to sustain higher levels of aggregate demand. Domestic factors behind the recent slowdown include production problems in the car manufacturing industry and uncertainty about fiscal and economic policies in some Member States. The fiscal stance is projected to turn expansionary in the euro area in 2019, while public debt continues to decline.

The degree and impact of the expected slowdown on the European economy will depend on our policy action. Promoting and protecting investment, in particular in people and skills, will simultaneously strengthen the growth potential of our economies and support aggregate demand. As regards public finances, governments should continue to improve their sustainability, in particular where debt ratios are high and Member States have not taken advantage of the favourable cyclical conditions and low interest rates to rebuild fiscal buffers. At the same time, fiscal space should be used where it exists, and specific attention should be paid to the growth-friendliness and redistributive effects of expenditure and the tax system. Finally, a more symmetric rebalancing across the euro area will contain the negative impact of deleveraging on growth and make our economic performance depend less on external demand.

In line with President Juncker's 2018 State of the Union address, the 2019 Annual Growth Survey called for more targeted investment policies coupled with a well-designed set of structural reforms and responsible fiscal policies. In addition, the recommendation for the economic policy of the euro area in 2019[1] stressed the need to complement national efforts with continued reforms at the European level, such as strengthening the Single Market. While policy action has been taken in recent years to improve the resilience of our economies, challenges remain. Growth in Europe is not

[1] COM(2018) 759 final.

benefiting all countries, regions and citizens in the same manner. Some Member States are still experiencing high unemployment, real household income below pre-crisis levels and high poverty rates. Regional differences remain large and are increasing within some Member States. In addition, total factor productivity growth is low and digital technologies continue to spread slowly. Combined with the impact of demographic ageing on our workforce, this will limit our growth potential in the future. The country reports published together with this Communication pay particular attention to how Member States deliver on the dimensions of the European Pillar of Social Rights. The implementation of the Pillar is a compass for achieving inclusive, fair and sustainable growth.

Going forward, in this Semester package, the Commission presents a more effective policy link between the European Semester and EU funding for 2021-2027, following the Commission's proposals for the next EU multiannual financial framework. The objective is to ensure greater coherence between the coordination of economic policies and the use of EU funds, which represent a significant part of public investment in several Member States (cohesion policy funds alone in the next programming period correspond to 0.5 % of EU GDP). To that end, country reports identify priority areas for policy action regarding public and private investment in Member States, and therefore provide the analytical basis for a successful programming of cohesion policy funds and use of related EU funds in 2021-2027.

2. PROGRESS WITH COUNTRY SPECIFIC RECOMMENDATIONS

The country reports published today provide the analytical basis for the country-specific recommendations in the European Semester. During this European Semester cycle and continuing from last year's efforts, the Commission intends to deepen the dialogue with Member States, social partners and other relevant stakeholders, to further encourage the implementation of country-specific recommendations and increase their ownership at national level. This dialogue would include dedicated visits to Member States and both bilateral, and multilateral, discussions.

All Member States have made progress with the implementation of the country-specific recommendations albeit to varying degrees. Since the start of the Semester in 2011, Member States have made at least 'some progress' with the implementation of more than two thirds of all the country-specific recommendations. This rate of progress is broadly stable compared to the Commission assessment in May 2018[2]. As was the case in previous assessments, Member States have made most progress in financial services, reflecting the priority given to the stabilisation and soundness of the financial sector in the aftermath of the financial crisis. Also, consistent with the initially large impact of the crisis on the labour market, sound progress has been achieved with the implementation of the recommendations to promote job creation on permanent contracts and to address labour market segmentation.

In view of the mounting economic risks, stronger reform implementation is crucial to strengthen the resilience of our economies. Member States need to make better use of the supportive economic conditions by further progressing with the implementation of the recommendations addressed to them by the Council in 2018. Most progress is achieved in the recommendations addressing challenges in the financial sector notably regarding the financial services, the reduction of private indebtedness, and the reform of insolvency procedures. At the same time, progress has been particularly weak in addressing competition and regulatory frameworks, as well as in addressing recommendations related to state-owned enterprises and in broadening tax bases. In some cases, there is some evidence of backtracking for instance in the area of long-term sustainability of public finances, including pensions.

Reforms and investment require sufficient administrative and technical capacity for Member States to deliver on expected results. Sound preparatory work by an administration that is appropriately staffed with the necessary technical means maximises the impact of public investments and reforms. Reforms of public administrations have limited short-term costs and can be effective at any point of the cycle. Achievable and measurable outcomes of reforms need to be specified, monitored, and communicated. The Structural Reform Support Programme offers hands-on technical support to all Member States, at their request, to design and implement reforms, especially for following up on the European Semester recommendations[3].

[2] Chapeau Communication of May 2018.
[3] The 2019 financing decision is adopted with this package.

3. ADDRESSING MACROECONOMIC IMBALANCES

The in-depth reviews in the country reports provide a comprehensive analysis of the imbalances experienced by the Member States. They identify underlying vulnerabilities and relevant cross-border implications. Macroeconomic imbalances can adversely affect the economy of a particular Member State, the euro area, or the Union as a whole. The macroeconomic imbalance procedure aims at detecting and preventing their emergence at an early stage to ensure that the Member States concerned take appropriate action to correct them.

The 2019 Alert Mechanism Report identified 13 Member States for an in-depth review to assess whether they are affected, or may be at risk of being affected, by imbalances[4]. Of those countries, 11 were considered to be experiencing imbalances or excessive imbalances already in 2018. In addition, after having exited the financial assistance programme, Greece was subject to an in depth review for the first time. The 2019 Alert Mechanism Report also considered that an in-depth review for Romania was warranted, in order to assess the implications of the ongoing deterioration in the country's cost competitiveness and external balance. The selection of Member States was supported by the Council[5]. The analysis looks at the gravity of the imbalances, their evolution and the policy response to the macroeconomic imbalance procedure related country-specific recommendations. Relevant spillovers and systemic cross-border implications of imbalances are also taken into account.

3.1. Progress with correcting the macroeconomic imbalances in the EU and the euro area

The correction of macroeconomic imbalances in the EU is progressing thanks to resumed growth and policy efforts, but vulnerabilities persist. Private and government debt stocks remain at historically high levels in certain Member States and their correction is not always proceeding fast enough. This reduces the room for absorbing future negative economic shocks. In addition, in a number of Member States signs of possible overheating are present, mainly linked to dynamic house price growth and fast-growing unit labour costs.

The rebalancing of external positions remains incomplete. Large current account deficits have been corrected in most Member States, but a few still face largely negative net international investment positions. Large stocks of external debt remain a vulnerability in a number of Member States, which need to maintain prudent current account positions and avoid competiveness losses. Other Member States exhibit instead large current account surpluses, which have remained rather persistent. Modest signs of adjustment have become visible only recently. Addressing large surpluses in net-creditor countries through investment and wage policies would contribute to support the growth potential. At aggregate level, the euro area current account surplus surpassed slightly 3% of GDP in 2016 and has remained broadly constant afterwards. This large surplus reflects a context where aggregate domestic demand in the euro area has been lagging behind economic activity and where the improved competitive position by the euro area economies has sustained exports.

Debt reduction is continuing. Making effective progress in reducing private and government debt levels would be key to create room to absorb future negative economic shocks. Private debt-to-GDP ratios are falling in an increasing number of Member States. This is mainly the result from higher nominal GDP growth. Debt reduction from positive net savings, as well as

[4] COM(2018) 758 final.

[5] https://data.consilium.europa.eu/doc/document/ST-5603-2019-INIT/en/pdf

from resuming credit growth, is becoming less intense and widespread. Corporate debt reduction has been faster than in the household sector, partly due to the low levels of investment these past several years. On the public sector side, while improved budgetary positions and resumed GDP growth are currently leading to reductions in government debt ratios in most Member States, they are nonetheless falling only slowly.

Conditions in the EU banking sector are improving especially in the most vulnerable countries, but further efforts are needed. Capital ratios have further improved in most Member States. Non-performing loan ratios have declined notably in some Member States where their stock is the highest. The EU average non-performing loan ratio stood at 3.3% in the third quarter of 2018 compared to 4.4% one year earlier, but these ratios remain very high in some Member States where additional efforts are needed. Capital and liquidity ratios have further improved in a broad majority of banks. Despite recent improvements, low profitability linked to overbanked markets remains a concern. Capital markets have also contributed further to broadening and diversifying the financing of the European economy. There is significant additional potential for their development at European, national and regional level.

House prices are accelerating in a growing number of Member States, with more countries exhibiting possible signs of overvaluation. House prices have risen faster in Member States that have shown no or only little evidence of overvaluation in recent years, and in some cases mortgage credit is resuming at higher pace. On the positive side, house prices have recently moderated in countries where the evidence of overvaluation is the highest, including stemming from affordability constraints and recently implemented macro-prudential policies.

Labour markets continue to improve. Unemployment rates are further declining, including for young people and the long-term unemployed, but remain high in some Member States. Wages in Member States are resuming at differentiated speeds that broadly reflect the extent to which some countries are experiencing labour shortages, while wage growth for the euro area as a whole remains below what would be expected at the current levels of unemployment on the basis of historical data.

Since 2016, unit labour costs in most Member States have been growing at faster rates than before. Strong accelerations have been recorded, especially in Member States with below-average wage levels, partly due to labour shortages. So far unit labour cost developments have not been matched by substantial losses in export market shares or deteriorations in current account balances but these effects could become visible if those trends persist. At the same time, within the euro area, the cost competitiveness advantage in countries with a legacy of large current account deficits or with still sizeable stocks of external debt has slowed-down, showing the need to keep the momentum for reforms aimed at increasing productivity growth and maintaining cost competitiveness.

3.2. Implementing the macroeconomic imbalances procedure

Imbalances or excessive imbalances have been identified in all Member States analysed in in-depth reviews, but the gravity of imbalances has narrowed in some cases. The 2019 in-depth reviews have found that 10 Member States are experiencing imbalances and three are experiencing excessive imbalances. One country has reached clear progress up to the point of improving its macroeconomic imbalance procedure categorisation to imbalances from excessive imbalances one year ago. In other cases the correction of economic imbalances is ongoing, but not sufficiently to justify an exit from the macroeconomic imbalance procedure. Appendix 3 summarises the findings from the in-depth reviews by Member State.

Greece, that has been integrated into the European Semester after exiting the stability support programme, has been identified as experiencing *excessive imbalances*. Greece still faces major challenges related to high public debt, negative net international investment position, a high share of non-performing loans, the still high unemployment rate and low growth potential. Deep institutional and structural reforms, initiated in recent years to modernise the economy and the State, have started to bear fruit as reflected by the successful conclusion of the European Stability Mechanism programme, the recovery of growth as well as the reduction of unemployment. This reform process requires sustained implementation for their impact to fully unfold. Since the exit from the programme Greece is subject to enhanced surveillance, which provides the basis for assessing the implementation of commitments undertaken by Greece to ensure the continuity and completion of reforms adopted under the European Stability Mechanism stability support programme.

Romania, identified with no imbalances in 2018, is found to be experiencing *imbalances*. Risks related to competitiveness losses and a widening current account deficit highlighted in the Alert Mechanism Report have been confirmed in the in-depth review. Moreover, recent legislative initiatives appear to be inducing risks to the financial sector. That is happening in a context of weakening reform implementation, unpredictable policy-making environment, and an expansionary fiscal policy. If not addressed, those patterns will impinge on government and foreign debt prospects and harm investment and growth prospects.

Croatia, identified with excessive imbalances in 2018, is found to be experiencing *imbalances*. Economic developments have been contributing to a gradual correction of existing imbalances, notably those related to high stocks of public, private and external debt, and in that way leading to a reduction of risks. Policy action and commitments that would help a sustainable correction of imbalances have been stepped up recently, and their full, swift and effective implementation will be crucial.

In other countries, economic developments have been generally favourable to the correction of imbalances, but challenges remain on the economic and policy outlook:

- Bulgaria, France, Germany, Ireland, the Netherlands, Portugal, Spain, and Sweden are identified, as in 2018, to be experiencing ***imbalances***. **Bulgaria** took further steps to ensure the stability of the banking sector but some actions are yet to be finalised or implemented. **France** has stepped up reform commitments but correction of imbalances related to high public debt and weak competitiveness dynamics crucially depends on policy progress. In **the Netherlands**, policy efforts have been stepped up but imbalances related to the high stock of private debt and the large current account surplus remain. In **Germany**, the current account surplus remains high and is decreasing only slowly while more efforts are needed to fill the investment gaps particularly as regards public investment in infrastructure and education. In **Ireland**, strong growth and policy progress have continued to support a narrowing of stock imbalances but vulnerabilities remain in a context of increased risks from the international environment. Remaining stock imbalances related to internal and external debt are receding in **Portugal** and **Spain** helped by improved economic conditions, although policy and adjustment gaps remain. In **Sweden**, imbalances persist despite some recent adjustment in house prices and policies.

- Cyprus and Italy are identified, as in 2018, to be experiencing excessive ***imbalances***. In **Cyprus**, despite an improved economic context and some recent stepping up of policy efforts, significant vulnerabilities persist related to a falling but still high level of non-performing loans and external, private and government debts. In **Italy**, progress in some policy areas in earlier years has been overshadowed by worsening prospects largely coming from the planned budgetary deterioration and a broadly stalled reform agenda. Recent policy measures backtrack on elements of previous reforms and will affect negatively the sustainability of public finances, productivity and potential GDP growth. Uncertainty related to the government stance contributed to increased market pressures and higher yields on sovereign debt in the course of 2018. The aggravation or alleviation of macroeconomic imbalances will crucially depend on policies to improve the quality of Italy's public finances, increase the efficiency of its public administration and justice system, enhance its business environment, and strengthen its labour market and the financial system. The Commission will therefore closely monitor developments in Italy and assess policy steps and commitments to address imbalances, in particular the level of ambition of the National Reform Programme, in the context of the forthcoming European Semester spring package.

The Commission will continue reviewing developments and policy measures taken by all Member States with imbalances or excessive imbalances in the framework of specific monitoring. The Council participates in those reviews and has supported the conclusions of the specific monitoring reports.[6]

Table 1: Outcomes of in-depth reviews in 2019 and situation in 2018

	Situation in 2018	Outcome of 2019 IDRs
Imbalances	BG, DE, ES, FR, IE, NL, PT, SE	BG, DE, ES, FR, HR, IE, NL, PT, RO, SE
Excessive imbalances	CY, HR, IT	CY, EL[7], IT

[6] https://data.consilium.europa.eu/doc/document/ST-5603-2019-INIT/en/pdf

[7] Like other countries that have exited a financial assistance programme in the past, Greece has been identified with excessive imbalances

4. MEMBER STATE POLICIES

In the context of slowing growth, effective reforms and well-targeted investment priorities would help Member States be more resilient to future macroeconomic shocks. With better functioning financial, product and labour markets and institutions and more efficient state administrations, our economies can adjust more smoothly and minimise economic and social costs. Whether it is because they create the necessary infrastructure, provide a better skilled labour force or support innovative entrepreneurial ideas, well-targeted investments strengthen potential growth in the longer term, contributing to competitiveness and economic resilience. Adapting to ongoing structural change would help economies converge by narrowing differences in productivity and would improve social outcomes.

4.1 Ensuring responsible fiscal policies and financial stability

Responsible fiscal policies, quality of public finances and growth-friendly tax systems

Member States with high debt ratios are failing to build fiscal buffers. Robust economic growth and historically low interest rates continue to support a decline in public debt ratios. In 2018, favourable cyclical conditions and declining interest expenditure resulted in a further decline of the overall budget deficit in the EU, which now stands below 1% of GDP. That downward trend is expected to end in 2019, when the overall deficit is projected to slightly increase for the first time since 2009. Public debt remains close to historical peaks in some Member States. The projected fiscal adjustment is relatively limited or even negative in some highly indebted Member States. Rebuilding fiscal buffers is especially important in Member States with still high levels of public debt with the view to reducing their vulnerability to shocks and allowing automatic stabilisers to operate fully in the next downturn. Compliance with the Stability and Growth Pact, along with some fiscal expansion by Member States with fiscal space would contribute to a balanced policy mix, given the continued support to the economy from monetary policy. Furthermore, it would reduce the risks of financial instability.

There is ample room to enhance the quality of public finance, and spending reviews are a crucial tool in this regard. Many Member States engage in a scrutiny of public spending, aimed at increasing its efficiency and making savings, creating room for growth enhancing expenditure. Broad spending reviews are planned in Italy and France. More targeted reviews, covering specific spending areas are foreseen in many other Member States. They encompass areas, like healthcare, education, state-owned enterprises, real estate, public investment, transport and environment. In 2019, efficiency gains should emerge in Portugal from a greater use of centralised procurement and more efficient use of public assets, and in Latvia from a more cost-efficient management of state-owned enterprises in the real estate sector and consolidation of the information technology infrastructure. Going forward, spending reviews would benefit from more frequent and rigorous interim evaluations as well as a tighter integration with the budgetary process.

Member States are continuing to improve their domestic fiscal frameworks, a key factor of fiscal policy-making. Fiscal frameworks have been considerably reformed over the past several years: the positive effects on government spending and taxation are already visible. Reforms in this direction continued recently in a number of Member States. In Germany, the Joint Economic Forecast Project Group has been mandated to endorse the macroeconomic forecasts. Hungary and Lithuania have further improved the medium-term perspective of their framework. Even Member States where fiscal frameworks usually serve as best practice continue to improve them. Notably, Sweden has introduced a new debt anchor, while the Netherlands has improved the automatic stabilisation features of its framework. Ireland is implementing its plans to set up a rainy-day fund. Nevertheless, there are still areas where more efforts are necessary. This in particular concerns coordination arrangements across the levels of government in Member States with complex federal structures.

An ageing population confronts many Member States with the challenge of ensuring the sustainability of their public finances. Over the past decade, significant progress has been made in addressing the projected increase in pension costs. However, rising longevity and the retirement of the baby boom generation still result in considerable projected increases in age-related expenditure for 21 Member States that face medium or high fiscal sustainability risks. This may have an impact on the future adequacy of pensions. In 2018, Croatia adopted a pension reform that is set to improve pension adequacy while not endangering long-term sustainability while France put forward comprehensive reform plans. Cases of partial backtracking risk undoing part of the progress made over the past decade in Italy and Romania. Measures that increase pension expenditure have been introduced or are being planned also in Germany, Spain and Portugal. Progress towards ensuring long-term fiscal sustainability appears slow for health care and long-term care. Current reform efforts in some Member States tend to be partial and should better combine the objectives of fiscal sustainability with accessibility and effectiveness of care.

Health system reforms are targeting greater effectiveness, accessibility and resilience. Many Member States are pursuing efforts to refocus health systems towards preventive care, whilst bolstering primary care and better coordination across care settings. Cyprus is putting in place a new system of health contributions paving the way for universal health coverage and limiting high out-of-pocket payments. Poland has started pilot projects to reinforce primary and ambulatory care and improve coordination.

Tax systems can help support inclusive growth. Growth-friendly tax systems can support private investment and improve the business environment, encourage employment and labour market participation, reduce inequalities and contribute to an environmentally sustainable economy. In that light, several Member States are continuing to reform their tax system and in particular reduce labour taxation. Latvia and Lithuania are introducing a progressive personal income tax rate schedule. The Netherlands is shifting the tax burden from labour to consumption by reducing personal income taxes and increasing value added tax rates. Germany and Ireland are continuing to reduce labour taxation for low- and middle-income earners. Denmark, Greece and Slovenia ensure a high share of environmental tax revenues, which encourages more efficient use of resources and boosts investment and employment.

The fight against aggressive tax planning is a priority to ensure the Single Market operates properly. The Commission has presented legislative proposals to make the tax system more transparent, effective and coherent and less prone to aggressive tax planning practices. Aggressive tax planning can have a budgetary impact on other Member States, distort the playing field among companies, and unfairly divert resources from governments' spending objectives. Member States whose tax base is eroded either must raise revenue from other taxes or have less revenue for growth-enhancing reforms and for redistribution purposes to fight inequalities. The transposition of EU legislation and of internationally agreed initiatives will help to curtail aggressive tax planning practices[8]. Aggressive tax planning can be further addressed by strengthening national tax legislation, increasing transparency and administrative cooperation.

[8]For example, by the end of 2018, all Member States had to transpose the provisions of the Anti-Tax Avoidance Directive ((EU) 2016/1164) into their national law.

Banking sector, low profitability and non-performing loans

On aggregate, bank capital and liquidity positions have continued to improve in 2018, supported by the economic environment as well as legislative and supervisory action. At the same time, bank leverage has decreased while loss-absorbing capacity has increased. Non-performing loans on bank balance sheets have continued to decline. The latest figures show that the gross non-performing loans ratio for all EU banks further declined to 3.3 % (Q3-2018), down by more than one percentage point year-on-year. Fourteen Member States had low non-performing loans ratios of below 3 %. There was in particular a significant reduction in Cyprus, Ireland, Italy, Spain, Portugal, Hungary, Slovenia, Romania, Austria and Germany, where the pace of non-performing loans disposals has picked up significantly since 2017 amid persistent supervisory pressure and/or a further development of secondary non-performing loans markets.

In addition, the legislative processes for several risk reduction measures at EU and national level continued to move forward resulting in tangible progress. The agreement of December 2018 between Council and Parliament with respect to the Risk Reduction package should continue to strengthen bank capital and liquidity positions, particularly in potential resolution scenarios, as well as to facilitate more risk reduction and risk sharing in the EU banking sector. This includes ensuring full implementation of EU rules against money laundering and adequate risk prevention and management by banks.

The European Banking Authority 2018 stress test confirmed that EU banks are becoming more resilient. Yet, investors perception of the tests may not lead to material changes in the way the market sees capital resilience of EU banks, whose share prices may continue to be more driven by macroeconomic fundamentals in 2019. Bank profitability remains subdued and affected by high non-performing loans ratios, inadequate business models in several cases, overbanked markets and financial market volatility (re-emerged since the first half of 2018).

Cross-border banking in the EU may accelerate again taking advantage of the announced restructuring needs of some large European groups. Some leading banking groups in key Member States are switching their strategies to reduce profitability risks. This might provide banks with opportunities to accommodate some of their profitability risks.

4.2 Labour market, education and social policies

The employment situation continues to improve. The number of people in employment hit a record 240 million in the fourth quarter of 2018. At 6.6% the unemployment rate is more than back to pre-crisis levels: it is at the lowest level ever recorded since the corresponding data started to be collected in 2000. Following years of economic growth and job creation, the social situation continues to improve. In 2017 alone, more than five million people were lifted out of poverty and social exclusion.

Yet, the situation points to significant differences across Member States. In some Member States unemployment rates have not fully recovered and are still above 10%. The situation of young people remains a challenge in some of the latter countries: high shares of young people neither in employment, nor in education or training raise concerns for their present and future employability. In others, there are increasing labour shortages creating a bottleneck for further growth. Overall, despite increasing employment rates among women, gender gaps in employment rates persist and lead to gaps in pay. Low qualified people and people with a migrant background in particular, face difficulties to find jobs. People with disabilities also remain at a disadvantage. Moreover, large regional disparities in labour market outcomes exist in many Member States.

Demographic changes and technological developments are reshaping European job markets. As the population ages and the number of young people declines, it is crucial for Member States to increase the number of people active on the labour market, to ensure strong growth potential as well as to ensure that social security systems are sufficiently and sustainably funded. Some Member States are taking action in this area. For instance, in Croatia, a pension reform entered into force in January 2019, aimed at promoting longer working lives and addressing structural inconsistencies in the system. Given the transformations that digitalisation and the spread of platforms are bringing to the future of work, it is crucial that Member States modernise labour markets and social protection systems, including by ensuring adequate social protection coverage to non-standard workers and self-employed, to keep pace with these developments.

Promoting adequate skills is crucial. Equal access to high-quality education is essential if all citizens are to fully participate in our societies and make the most of their working lives. Adequate skills can increase productivity and potential growth, which are key to allow for wage growth and improve social and living conditions. In a context of rising skills shortages and mismatches, education and training systems need to be strengthened and modernised. At the same time, re-skilling and upskilling policies are important to increase the resilience and adaptability of the workforce, to prevent that low-skilled people and people with a migrant background are faced with deteriorating chances of employment. France is implementing reforms to better link the education and training system to labour market needs. Latvia is taking action to improve the quality, attractiveness and labour market relevance of the vocational education and training. In Portugal, the Qualifica programme aimed at tackling the challenge of a low-qualified labour force, has been recently reinforced through a reprogramming of the European Social Fund allocations. A number of Member States (Germany, Austria, Sweden, Finland, Belgium) took measures to validate, recognise or improve existing skills of migrants in order to facilitate their labour market integration.

Labour market segmentation remains a challenge. Although the share of temporary employees, on average, has not increased substantially in recent years, some Member States are experiencing rates persistently above 15 %. In countries such as Spain, Slovenia, Poland, Portugal, Italy and Croatia over 60 % of temporary employees are young people. More than half of the employees on a temporary contract cannot find a permanent position and while the total number of hours worked has only recently returned to pre-crisis levels, the share of involuntary part-timers still exceeds 50 % in some Member States. Several Member States are taking action to promote open-ended hiring by reforming labour law enforcement, including increasing the staffing of labour inspectorates to tackle the misuse of temporary work and promoting a better design of hiring subsidies. In Spain, the capacity of labour inspectorates to fight the abuse of temporary contracts and undeclared work was further strengthened in 2018. Cyprus is taking significant actions to support regular employment, with the establishment of a Single Inspections Service. In Ireland, a new bill requires employers, among other things, to provide better information on the nature of employment.

Wages are growing at a moderate pace but faster than in previous years. Nominal compensation per employee grew by 2.7 % in 2018. Wage growth has caught up with productivity developments, after having trailed behind for some years.

Poverty and income inequality declined in 2017, but in-work poverty remains a source of concern. The share of people at risk of poverty or social exclusion declined to 22.4% in 2017 and is now below pre-crisis levels, however some groups are characterised by a persistently higher risk of poverty. Moreover, in-work poverty remains a source of concern being particularly high for self-employed, temporary and part-time workers and for workers who are not born in the EU. The tax and benefits system plays an important redistributive role. It is important to target carefully poverty support to those most in need, e.g. by reinforcing the accuracy of means testing instruments. In Luxembourg, a new social inclusion income scheme replaced the previous guaranteed minimum income with the aim to promote social inclusion and activation, and to tackle poverty of children and single-parent families. Italy adopted a new minimum income scheme (*Reddito di Cittadinanza*) that will replace the previous one, with the aim to develop an active inclusion model. Its success largely relies on the effectiveness of its governance.

Well-functioning social dialogue is key to improving the design and implementation of reforms, to increase ownership. Over the last year, social partners in a number of Member States reported positive developments regarding the meaningful and timely engagement of their government on economic and social reforms. For instance, based on a tripartite agreement, Portugal put forward a set of measures to address labour market segmentation, which now has to be legislated. Positive development in some Member States contrasts with steps back in others. In many of them, there is scope for improving social partners' capacity and timely consultation at key stages of designing reform measures, including at important milestones of the European Semester.

4.3 Competitiveness and productivity

Addressing the productivity gap

Against the backdrop of demographic trends, productivity growth is key to ensuring future sustainable growth in all Member States. Productivity has been growing slowly in the EU. The causes are varied, including inter alia low investments in research, technology and innovation and the structural shift from manufacturing to services. Addressing sluggish labour productivity is essential to address EU's short and long-term economic challenges. Growth in labour productivity is likely to remain low at around or below 1% in the coming years, and there are notable differences in productivity across Member States. In particular, mature economies with already high productivity levels are finding it difficult to raise their growth potential. Investment that enhances environmental sustainability has the potential to boost productivity across the economy through enhanced resource efficiency and reduced input costs, whilst reducing external costs and impacts.

Productivity in the services sector (which accounts for the largest part of economic activity) remains relatively low despite the overall improved economic performance. While the productivity slowdown has been common to other advanced economies, the productivity gap in services remains large and growing, especially with the USA. This represent a disadvantage to EU companies for trade in general and for their integration in global value chains. To analyse the drivers of productivity and support an adequate policy response, the Council has recommended euro area Member States to set up national productivity boards.[9]

Higher labour productivity will make higher wages and potential output possible but this is not sufficient in itself to achieve those objectives. While there is evidence of higher productivity being passed on to wages in the mid and long run, there are also examples of labour earnings not keeping up with changes in productivity over time. Member States are thus taking additional measures to translate higher labour productivity into higher labour earnings.

Quality investment and a more effective use of EU funds

Well-targeted investment remains essential to address the challenge of productivity growth in the EU. It is one of the three essential elements of the "virtuous triangle" put forward by this Commission. Addressing investment needs has thus been a longstanding priority of the European Semester. In the current phase of the business cycle, the focus should be on public and private investment that increases productivity and growth potential while it will be important to protect investment in case economic risks were to materialise. Also long-term investment measures, including in skills and education, can help ensure that the EU economy enjoys sustainable growth and stays resilient, and it can also meet urgent social needs.

Investment in research, development and innovation is needed in most Member States to enhance their productivity growth and competitiveness. In many Member States and regions there is a significant scope to strengthen links between businesses, academia, research and public sector actors trough cooperation in value chains, including through smart specialisation. This is the case for instance in Belgium, Bulgaria, France, Cyprus, Poland, Latvia and Estonia. Moreover, digitalisation of companies and digital public services need further investment in Belgium, Cyprus, Austria, Slovenia, Spain, Slovakia, Poland, Estonia, Germany, and Bulgaria. Member States with higher productivity levels, such as Germany and the Netherlands, and others that have undergone significant structural changes with high investment rates before the crisis and during the recovery, such as Hungary, Poland and the Czech Republic, can make further progress by investing in intangibles and innovation. In catching-up Member States, investments in machinery and equipment can contribute to capital deepening and higher labour productivity. In order to respond to challenges linked to the circular economy and climate adaptation, investment related to resource efficiency and climate risk prevention is needed in Estonia, Luxembourg, Slovakia, Portugal, Bulgaria, the Netherlands, Italy, Cyprus, and France.

Better aligning EU funds with the European Semester analysis and recommendations should improve outcomes and strengthen the impact of cohesion policy funding. Aligning EU funds with the European Semester is a key component of the proposals for the multiannual financial framework for 2021-2027. For some Member States, EU funds even represent a critical part of their public investment. In particular, as put forward in the

[9] Council Recommendation of 20 September 2016 on the establishment of National Productivity Boards. OJ C 349, 24.9.2016, p. 1.

Commission's multiannual financial framework proposal, the European Regional Development Fund, the European Social Fund Plus and the Cohesion Fund would amount to around EUR 600 billion over the next programming period, if national co-financing is included — this corresponds to 0.5 % of EU GDP, and significantly more in the main recipient Member States. Moreover, the Commission's multiannual financial framework proposals allow combining these funds with other sources of EU funding, such as the future EUR 650 billion InvestEU Programme, the successor to the Juncker Plan. They have the potential to crowd-in other public and private investors and increase the investment impact in strategic areas of the EU economy even further.

Based on the analysis in the country reports, a new annex identifies how those EU funds could better help to address specific needs in Member States. In addition to a stronger focus on investment priorities, this year's country reports also have a more granular analysis of the regional disparities and bottlenecks to investment. The dedicated annex helps in the dialogue with individual Member States on defining the funding priorities of the future programmes implementing these funds. What is presented in the country reports constitutes the views of the Commission, based on the underpinning Semester analysis. It is the starting point for negotiations with the Member States on the programmes. It leaves space for flexibility in the discussions with Member States. That identification of investment needs is based on the shared understanding that investments should have as high an impact on economic, social and territorial cohesion as possible.

Private investment, sourced from well-functioning and integrated capital markets, needs to be more fully exploited. As the EU finalises the delivery on its action plan on building a Capital Markets Union, Europe's full diversity of capital markets ranging from global hubs to regionally integrated networks and local initiatives should be further developed to finance businesses, and promote decarbonisation and the transition to a more sustainable economy. At the national level, for example Estonia, Latvia and Lithuania are creating a pan-Baltic market for covered bonds and securitisation. This will contribute towards well-functioning and deeper capital markets in the region. It will also open up long-term funding options for banks, so they can free up their balance sheets to enable increased lending.

Institutional quality as a key factor for reform

Satisfying investment needs requires a favourable investment environment. Policy makers need to devote particular attention to creating an investment-friendly environment, avoiding unnecessary market and regulatory barriers and improving the way in which their public institutions and administrations operate. Aspects related to the effectiveness of the public administration, the degree of digitisation of public services, the quality and stability of the regulatory environment and the respect for the rule of law, including the independence of justice systems and the fight against corruption, have a critical impact on investment decisions. In 2019, about half of the top 25 performers in the world as regards corruption perception levels are EU Member States, but large discrepancies remain[10] and efforts to improve prevention of corruption, protect whistle-blowers to enhance detection and remove obstacles to effective prosecution and sanctions need to be stepped up. To address some of these challenges, Italy, Slovakia and Latvia have revised their whistle-blower protection regime, while Lithuania, Spain, Cyprus and Greece are currently envisaging reforms in this area.

[10]All Member States are subject to ongoing assessment of their anti-corruption efforts. As last year, the Commission has analysed the key challenges in the country reports in relevant Member States.

As reported in the 2019 country reports, all Member States experienced barriers to investment in different policy areas (see Appendix 4). Overall, weaknesses in public administration and the business environment account for the highest share of investment barriers. Examples include high regulatory and administrative burden, the lack of predictability in regulatory frameworks, the effectiveness of justice systems and inefficient public administration. Many barriers are also related to cumbersome and lengthy approval procedures as well as skill shortages due to weaknesses in education and training systems. Establishment barriers in retail have delayed cross-border investments in this sector. Skills shortages are mentioned in several country reports as barriers hampering and delaying investments in sectors that are driven by digitalisation and new technologies (e.g. telecommunications, connectivity or circular economy) but also in more traditional sectors facing growing demand (e.g. construction).

Reforms to improve the quality of governance, institutions, the effectiveness of justice systems and public administration are the basis on which advanced democratic societies operate and are of considerable economic importance. Such reforms can help to improve the environment in which firms and stakeholders operate and encourage business activity, reduce corruption and strengthen the respect for the rule of law. Among the most frequently cited impediments to investment in the EU are inefficiencies in public administration, unfavourable conditions for doing business, and high administrative and regulatory burden for specific sectors. In some Member States, investment is also held back by a lack of transparency in the public sector, complex tax systems, distorted product or labour markets and weaknesses in research and innovation frameworks and in institutions. To address issues like these, Poland has adopted a 'Constitution for Business', a comprehensive set of five laws to improve the business environment. France is implementing a broad agenda reform to improve the business environment and the competitiveness of French firms. Several Member States, such as Finland and Estonia, are making efforts to reduce administrative burden. Bulgaria, Slovakia, the Czech Republic, Slovenia, and Romania are currently reforming their public procurement systems. In 2018 the German federal government announced that it will create an agency for the promotion of disruptive innovation.

Withdrawal Agreement between the EU and UK

This package does not speculate on the economic risks associated with different Brexit scenarios.

Given the ongoing ratification process of the Withdrawal Agreement in the EU and the UK, projections for 2019 and 2020 are based on a purely technical assumption of status quo in terms of trading relations between the EU 27 and the UK. In the case of a "hard Brexit" which the Commission considers undesirable, but for which the EU 27 is well prepared[11], these assumptions would have to be revised downwards.

[11]COM(2018) 556 final/2 (corrigendum adopted on 27 August 2018); COM(2018) 880 final; COM(2018) 890 final.

5. NEXT STEPS

In recent years the European Union has moved from economic recovery to solid expansion and for 2019 Europe's economy is set to continue expanding notwithstanding the more uncertain outlook projected. To ensure such a continued economic expansion, Member States will need to implement effective structural reforms, engage in responsible fiscal policies and lay out targeted investment strategies. The more effective link between the European Semester and EU funding for 2021-2027 as presented in this year's Semester package will provide the necessary structure to ensure the effective delivery of the most targeted investment priorities.

The European Semester offers the Commission, Member States, social partners and stakeholders at all levels the opportunity to engage in a permanent dialogue with one another throughout the year. The country reports published with this Communication draw on in-depth exchanges with governments, national authorities and stakeholders at both technical and political level, including bilateral meetings held in December 2018. Their findings will be presented in the Commission's representation offices in the capitals of the Member States, and will be followed up in further bilateral and multilateral meetings.

The Commission will soon engage in the dialogue with Member States on the 2021-2027 programmes for the cohesion policy funds, informed by the investment-related findings and conclusions of the country reports. Commission Vice-Presidents and Commissioners will visit Member States to seek the views of parliaments, governments, social partners and other stakeholders on the analysis and conclusions of the country reports. The Commission will also discuss the summary findings of the country reports with the European Parliament.

In the light of the challenges identified, the Member States will present their economic and social priorities in their national reform programmes by mid-April. They will also present their multiannual strategies for sound public finances, in the form of stability (for euro area Member States) and convergence (for non-euro area) programmes. To provide an appropriate and sustainable response to the challenges, the Commission recommends that those programmes would be prepared with the involvement of all key stakeholders, such as social partners, regional and local authorities, and civil society organisations as appropriate.

APPENDIX 1 - INTEGRATED SURVEILLANCE OF MACROECONOMIC AND FISCAL IMBALANCES

	Macroeconomic Imbalances Procedure (MIP12)	Stability and Growth Pact[13] (MTO: medium term objective / EDP: excessive deficit procedure)	Comments
AT		Preventive arm Not at MTO; subject to debt rule[14]	Distance from MTO in 2018 less than allowance granted for unusual events
BE		Preventive arm Not at MTO; subject to debt rule	
BG	Imbalances	Preventive arm Achieving MTO	
CY	Excessive imbalances	Preventive arm Achieving MTO; subject to transitional debt rule[15]	
CZ		Preventive arm Achieving MTO	
DE	Imbalances	Preventive arm Achieving MTO; subject to debt rule	
DK		Preventive arm Achieving MTO	
EE		Preventive arm Not at MTO	
EL	Excessive imbalances	Preventive arm Subject to transitional debt rule	Since Greece was exempt from submitting Stability Programmes while it was under the programme, it has not yet nominated its medium-term objective.
IE	Imbalances	Preventive arm Achieving MTO; subject to transitional debt rule	
ES	Imbalances	Corrective arm Excessive deficit, deadline for correction 2018	Subject to transitional debt rule in 2019 conditional on the abrogation of the EDP based on validated outturn budgetary data for 2018.
FR	Imbalances	Preventive arm Not at MTO; subject to transitional debt rule	
HR	Imbalances	Preventive arm Achieving MTO; subject to debt rule	
HU		Preventive arm Subject to significant deviation procedure; subject to debt rule	
IT	Excessive imbalances	Preventive arm Not at MTO; subject to debt rule	
LT		Preventive arm Achieving MTO	
LU		Preventive arm Achieving MTO	
LV		Preventive arm Not at MTO	
MT		Preventive arm Achieving MTO	
NL	Imbalances	Preventive arm Achieving MTO	

[12] Both the 'imbalances' and 'excessive imbalances' categories entail specific monitoring, to be modulated depending on the severity of the challenges.
[13] The achievement of the MTO and the applicability of the (transitional) debt rule refer to 2018 based on the Commission 2018 autumn forecast.
[14] Debt rule: If the 60% reference for the debt-to-GDP ratio is not respected, the Member State concerned will be put in the Excessive Deficit Procedure, after taking into account all relevant factors and the impact of the economic cycle, if the gap between its debt ratio and the 60% reference is not reduced by 1/20th annually (on average over three years).
[15] Transitional debt rule: each Member State in the Excessive Deficit Procedure is granted a three-year period following the correction of the excessive deficit for meeting the debt rule. This does not mean that the debt rule does not apply during this period as Member States should make sufficient progress towards compliance during this transitional period. A negative assessment of progress made towards compliance with the debt benchmark during the transition period could lead to the opening of an Excessive Deficit Procedure.

PL		Preventive arm Not at MTO	
PT	Imbalances	Preventive arm Not at MTO; subject to transitional debt rule	
SI		Preventive arm Not at MTO; subject to transitional debt rule	
SE	Imbalances	Preventive arm Achieving MTO	
SK		Preventive arm Not at MTO	
RO	Imbalances	Preventive arm Subject to significant deviation procedure	
FI		Preventive arm Not at MTO; subject to debt rule	Distance from MTO in 2018 less than allowance granted for unusual events and structural reforms
UK		Preventive arm Not at MTO; subject to transitional debt rule	

(*) The Recommendations under the '2-pack' (Reg. No 473/2013) regarding measures to be taken in order to ensure a timely correction of its excessive government deficit only concern euro area Member States.

APPENDIX 2: PROGRESS TOWARDS EUROPE 2020 TARGETS

Europe 2020 targets for the EU	2010 data	Latest available data	In 2020, based on recent trends
1. Increasing the employment rate of the population aged 20-64 to at least 75 %	68.6 %	73.5 % (Q3 2018)	Target likely to be met
2. Increasing combined public and private investment in R&D to 3 % of GDP	1.93 %	2.07 % (2017)	Target unlikely to be met
3a. Reducing greenhouse gas emissions by at least 20 % compared to 1990 levels	14.2 % reduction	22 % reduction	Target likely to be met
3b. Increasing the share of renewable energy in final energy consumption to 20 %	12.5 %	17.5 % (2017)	Target likely to be met
3c.Moving towards a 20 % target in energy efficiency	11.8 % (distance to 2020 target for primary energy consumption)	5.26 % (2017)	Target likely to be met
4a. Reducing the rate of early leavers from education and training (ages 18-24) to less than 10 %	13.9 %	10.6 % (2017)	Target likely to be met
4b. Increasing the share of the population aged 30-34 having completed tertiary education to at least 40 %	33.8 %	39.9 % (2017)	Target likely to be met
5. Lifting at least 20 million people out of the risk of poverty and social exclusion	1.4 million increase (compared to the 2008 base year)	5.2 million decrease (compared to the 2008 base year) in 2017	Target unlikely to be met

APPENDIX 3 — FINDINGS FROM IN-DEPTH-REVIEWS BY MEMBER STATE

Bulgaria is experiencing imbalances. Vulnerabilities in the financial sector are coupled with high indebtedness and non-performing loans in the corporate sector. The net external position has improved on the back of robust growth and large current account surpluses. Steps have been taken to strengthen the stability of the financial sector. Banks and other financial corporations have made further progress in implementing the recommendations addressed after the asset quality and balance sheet reviews and supervision has been strengthened. However, fragilities linked to weak governance, asset quality and supervision remain, while new challenges are emerging in the insurance sector. The robust growth has supported continuous private deleveraging and further decreases in non-performing loan ratios, but stocks of non-performing loans in the corporate sector are still elevated. While there is progress in addressing sources of imbalances, the full implementation and monitoring of recent reforms to supervision and governance in the bank and non-bank financial sectors will be crucial. More action is also needed to reduce the stock of non-performing loans and to complete the reform of the insolvency framework.

Cyprus is experiencing excessive imbalances. A very high share of non-performing loans burdens the financial sector and high stock of private, public, and external debt hangs on the economy, in a context of still relatively high, even though declining, unemployment and weak potential growth. The current account deficit is significantly negative, even taking into account the presence of special purpose entities, reflecting strong domestic demand as well as the negative saving among households, and is not adequate to guarantee a sustainable adjustment of the large stock of net external liabilities. Deleveraging of private sector debt is ongoing but only slowly. New lending to the private sector remains limited. The transfer of a significant portfolio of non-performing loans from the Cyprus Cooperative Bank to the public sector in the context of the bank's sale and wind-down reduced significantly the share of non-performing loans in the banking system. However, non-performing loans remain high for both households and corporations. The government support in the sale of the Cyprus Cooperative Bank had a one-off increasing impact on public debt in 2018. Looking forward, the high public debt is expected to be on a declining path on the back of a continued strong fiscal performance. Compared to last year, the reform momentum has been stepped up especially on the front of measures to address the vulnerabilities from non-performing loans, but more progress is needed on structural reforms to increase the growth potential.

Germany is experiencing imbalances. The high and slowly declining current account surplus reflects a subdued level of investment relative to saving in both the private and the public sector and has cross-border relevance. This is in spite of an increasing need for investment and innovation to make the German economy more resilient and to ensure a sustainable and inclusive growth model. The surplus slightly narrowed in 2018 in the context of a pick-up in domestic demand and is expected to continue to decline gradually in the coming years while remaining at a historically high level. Private and public investment have increased noticeably and there is a shift towards more domestic demand-driven growth. Yet investment but also consumption remain muted as a share of GDP despite the favourable financing conditions, the persistent infrastructure and education investment needs, especially at municipal level and the available fiscal space. The budget surplus grew in 2018 and the debt ratio declined further. Wage growth increased somewhat with the tightening labour market, yet real wage growth remains modest. While a number of measures have been taken to strengthen private and public investment, more efforts are needed to clear the large investment gap particularly as regards public investment in infrastructure and education. There has been less progress in other policy areas.

Greece is experiencing excessive imbalances. Vulnerabilities are linked to high government indebtedness, the negative external position, the high share of non-performing loans, incomplete external rebalancing, in a context of high although declining unemployment and low potential growth. Greece managed to successfully exit the European Stability Mechanism support programme in August 2018 after making substantial improvements in recent years. Nonetheless, large stock imbalances remain, including a deeply negative net international investment position that is still deteriorating amid moderate nominal GDP growth and a current account balance that remains negative. There have been considerable improvements in cost competitiveness in past years which stalled recently in light of subdued productivity growth. While the level of public debt remains high, it is mostly held by the official-sector creditors and financing needs will be relatively low for at least a decade. The pace of debt reduction crucially depends on the continued achievement of the agreed fiscal targets and implementation of reforms to generate a sustainable increase in the growth potential. The financial sector is vulnerable due to a very large stock of non-performing loans and a low profitability, hampering credit growth and the recovery of investment. Private debt is decreasing while active deleveraging is still ongoing. Wide-ranging measures were taken during the financial assistance programmes to address many of the structural weaknesses of the Greek economy. On top of consolidating earlier reforms and adjustment efforts, the authorities have committed to ensure continuity and completion of reforms, which are monitored in the framework of enhanced surveillance.

Ireland is experiencing imbalances. Large stocks of private and public debt and net external liabilities constitute vulnerabilities. However, stock imbalances are under substantial correction. The activities of multinational firms with little connection to the domestic economy heavily influence net foreign liabilities which are falling on the back of large current account surpluses. The stock of private debt remains high but economic growth continues to support private deleveraging. The activities of multinational enterprises continue to influence corporate debt. Household debt appears broadly in line with fundamentals although it is high compared with disposable income. Government debt is projected to remain on a downward trajectory, while the deficit is moving closer to a balanced position. House prices have been growing at a rapid pace for a number of years but have slowed down recently. House prices are largely driven by supply constraints and there is no clear evidence of overvaluation. The stock of non-performing loans, although still high, has decreased further even if long-term arrears are falling at a slower pace. Policy action addressing these vulnerabilities has been taken, notably in the field of housing supply and macroprudential policy, but some measures will take time to generate the expected effects.

Spain is experiencing imbalances. Though economic growth remains robust, large stocks of external and internal debt, both public and private, continue to constitute vulnerabilities in a context of, still high unemployment and have cross-border relevance. The rebalancing in the external sector has continued even if the current account surplus weakened in 2018, reflecting factors linked to the global environment. Sustained current account surpluses over an extended period of time will be needed to bring net external liabilities down to prudent levels. Debt reduction for the private sector also progressed, on the back of robust nominal growth. The non-performing loans ratio has decreased further. Public debt has decreased slightly, with narrowing deficits forecast to support its further gradual reduction. Still, further efforts will be needed to bring public finances onto a more sustainable path. Unemployment has continued its decline, but remains high. Implementation of policy action to raise potential growth has been slow. Challenges remain, in particular concerning labour market segmentation, research and innovation, and business regulation, notably for services.

France is experiencing imbalances. Vulnerabilities stem from high public debt and weak competitiveness dynamics in a context of low productivity growth, which carry cross-border relevance. Government debt was broadly stable in 2018, although at an elevated level. It is forecast to recede only marginally. The high level of public debt reduces the fiscal space available to respond to future shocks and weighs on growth prospects. Unit labour cost increases continue to be moderate in a context of low productivity growth. Some elements of the business environment still weigh on non-cost competitiveness. Reforms have been taken in recent years, with progress on several fronts including labour markets, taxation and business environment. However, the effects of these reforms still have to fully materialise while further action is warranted in other fields, such as the reform of the unemployment benefit system, the reform of the pension system, and the spending review to ensure the sustainability of public finances and to enhance the growth potential.

Croatia is experiencing imbalances. Remaining vulnerabilities are linked to high levels of public, private and external debt in a context of low potential growth. However, they have been narrowing over the past years. This was supported by robust nominal growth, above estimated potential, and a prudent fiscal policy. The negative net external position remains large, but has been improving due to continued current account surpluses. Private sector deleveraging is ongoing, though its pace is set to abate as credit growth and investment recover. The budget balance has been in surplus since 2017 and public debt has declined notably since its 2014 peak. The financial sector is well-capitalised and profitable while non-performing loans, although declining, remain elevated. The foreign currency exposure of corporations and households has reduced, but remains a vulnerability. Policy action has been stepped up with the adoption of a pension reform and new legislation to improve the fiscal framework. Other relevant policy measures are in the pipeline and their thorough implementation remains crucial for strengthening the resilience of the economy.

Italy is experiencing excessive imbalances. High government debt and protracted weak productivity dynamics imply risks with cross-border relevance, in a context of still high level of non-performing loans and high unemployment. The government debt ratio is not expected to decline in the coming years, as the weak macroeconomic outlook and the government's current fiscal plans, though less expansionary than its initial plans for 2019, will entail a deterioration of the primary surplus. Cost competitiveness is stable, but weak productivity growth persists. This is rooted in long-standing issues with the functioning of labour, capital and product markets, compounded by weaknesses in the public administration and justice system, which drags down potential GDP growth. The stock of non-performing loans has continued to decline significantly, but maintaining the pace of reduction of non-performing loan could prove challenging given market conditions. Higher sovereign yields compared to the levels of early 2018 are affecting banks' funding costs and capital buffers weighing on lending to the rest of the economy and on GDP growth. Despite some progress in banks' balance sheet repair, insolvency reforms and active labour market policies, the reform momentum broadly stalled in 2018. The 2019 budget includes policy measures that reverse elements of previous important reforms, in particular in the area of pensions, and does not include effective measures to increase potential growth.

The Netherlands is experiencing imbalances. The high stock of private debt and the large current account surplus constitute sources of imbalances, with cross-border relevance. The surplus peaked in 2017 at a very high level, and it is expected to decline gradually although remaining very elevated. Part of the external surplus can be attributed to statistical features linked to the role of multinational companies and is not expected to attenuate in the near future. Supported by economic growth, the private debt-to-GDP ratio has continued its downward trend both for corporate and households, although remaining elevated. Nevertheless, nominal household debt is slowly increasing on the back of dynamic house price growth. Wage growth has so far been moderate despite the tightening labour market. Recent reforms, such as the speeding-up of the reduction of mortgage interest deductibility, are expected to reduce the debt bias for households, while fiscal stimulus is expected to contribute to support aggregate demand.

Portugal is experiencing imbalances. The large stocks of net external liabilities, private and public debt, and a high share of non-performing loans constitute vulnerabilities in a context of low productivity growth. The current account is broadly balanced but a continued prudent position and the maintenance of competitiveness gains are required to ensure the adjustment of net external liabilities to prudent levels. Private debt ratios continue to decline from high levels on the back of nominal growth with a reduced role of active deleveraging. Government debt started declining as from 2017 backed by primary surpluses while remaining elevated. Risks in the banking sector have diminished including in light of recapitalisations of major banks in 2017 and a recent improvement in profitability. The large stock of non-performing loans has decreased but remains comparatively high. Ensuring higher productivity growth is key for improved prospects in competitiveness, deleveraging and potential growth. The labour market adjustment has progressed further and unemployment has been decreasing at a strong pace for several years. There has been policy action to address the level of non-performing loans but policy gaps remain in other areas, such as product and service markets. The adoption and implementation of several reform plans, including fiscal-structural reforms to improve the sustainability of public finances, will need to be monitored.

Sweden is experiencing imbalances. Overvalued house price levels coupled with a continued rise in household debt poses risks of a disorderly correction. The high household debt has continued to grow as a share of GDP. There has been a correction of house prices in the second half of 2017 which have since then gradually stabilised. Nevertheless, valuation indicators suggest that house prices remain high relative to fundamentals. Although the banking sector appears adequately capitalised, a disorderly correction would negatively affect the financial sector given the large exposure to household mortgages. In such a case, there could also be negative spill-overs to neighbouring countries given the systemic financial interlinkages. Structural bottlenecks for housing supply persist and construction output has weakened. Although measures have been taken in recent years in the macro prudential field to address mortgage debt growth, the impact appears so far limited. Key policy gaps remain, particularly in relation to tax incentives for home ownership and the functioning of housing supply and the rental market.

Romania is experiencing imbalances. Vulnerabilities are linked to cost competitiveness losses and a widening current account deficit in a context of an expansionary fiscal policy and an unpredictable business environment. Recent legislative initiatives create risks for the functioning of the financial sector and may harm private investment. The current account deficit has been growing on the back of buoyant imports, mainly for consumption purposes, and is forecast to widen further. The strong nominal GDP growth has nevertheless implied that the negative Net International Investment Position has been improving for some years but this may stall with the persistency of the current account deficits and lower GDP growth looking forward. Demand is fuelled by strong wage growth, inter alia linked to hikes in public wages and the minimum wage, which has translated into very substantial increases in unit labour costs. Despite cost competitiveness losses, so far export market shares have been growing. The expansionary fiscal stance, in a context of strong GDP growth, is forecast to continue thus contributing to buoyant private consumption dynamics. After declining for some years, the government debt ratio is projected to increase. Frequent and unpredictable legislative changes contribute to a weaker and uncertain business environment, with negative repercussions on business decisions and investment. Recent legislative initiatives with impact on banks' risk threaten the functioning of the financial sector and may hinder investment through both a tighter credit market and a shallower capital market with weaker institutional investors. In other areas, progress with reforms has slowed down or reversed.

APPENDIX 4 — INVESTMENT BARRIERS IN MEMBER STATES

	Investment Challenges	AT	BE	BG	CY	CZ	DE	DK	EE	EL	ES	FI	FR	HR	HU	IE	IT	LT	LU	LV	MT	NL	PL	PT	RO	SE	SI	SK	UK
Public administration/ Business environment	Regulatory and administrative burden	■	■	■	■	■	■				■	■	■	■	■		■		■	■	■			■	■			■	
	Public administration			■	■	■	■					■		■	■		■	■		■	■		■	■	■			■	
	Public procurement /PPPs	■		■	■	■	■				■			■	■		■	■		■			■	■	■	■	■	■	
	Judicial system			■	■						■			■			■				■		■	■	■		■	■	
	Insolvency framework			■	■				■		■			■	■		■	■	■	■	■				■			■	
	Competition and regulatory framework				■			■							■		■	■		■			■		■		■		
Labour market/ Education	EPL & framework for labour contracts				■						■		■				■	■						■					
	Wages & wage setting										■	■	■	■			■							■					
	Education, skills, lifelong learning		■	■			■		■		■			■	■	■	■	■		■	■		■	■	■			■	■
Fin. Sect. / Taxation	Taxation	■	■			■	■				■		■		■	■	■			■			■	■	■				
	Access to finance	■	■	■	■						■			■		■	■	■		■	■			■	■		■		
R&D&I	Coop. between academia,research & business			■	■	■		■	■		■	■			■	■	■	■	■	■			■	■	■	■			
	Financing of R&D&I					■	■		■		■		■			■	■	■			■	■		■	■				
Sector specific regulation	Business services / Regulated professions	■	■				■				■		■	■	■	■	■		■					■			■		
	Retail		■				■	■			■	■					■												
	Construction			■	■	■		■				■				■	■		■	■	■	■	■		■	■	■	■	■
	Digital Economy / Telecommunications			■			■				■		■	■		■									■				■
	Energy		■	■	■		■					■	■	■				■		■			■	■	■			■	■
	Transport		■			■	■							■							■		■	■	■		■	■	■

■ Barrier to investment

*: Until 2018, EL has been under Economic Surveillance Programme and it was not included in the 2015 exercise on barriers to investment. In 2018, there were no CSRs because EL was not included in the Semester.