Council of the
European Union

Brussels, 25 March 2024
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LEGISLATIVE ACTS AND OTHER INSTRUMENTS

Subject:	COUNCIL RECOMMENDATION on the economic policy of the euro area

COUNCIL RECOMMENDATION (EU) 2024/…

of …

on the economic policy of the euro area

THE COUNCIL OF THE EUROPEAN UNION,

Having regard to the Treaty on the Functioning of the European Union, and in particular Article 136 in conjunction with Article 121(2) 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 Regulation (EU) No 1176/2011 of the European Parliament and of the Council of 16 November 2011 on the prevention and correction of macroeconomic imbalances[2], and in particular Article 6(1) thereof,

Having regard to the recommendation of the European Commission,

Having regard to the conclusions of the European Council,

Having regard to the opinion of the Economic and Financial Committee,

Having regard to the opinion of the Economic Policy Committee,

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1 OJ L 209, 2.8.1997, p. 1, ELI: http://data.europa.eu/eli/reg/1997/1466/oj.
2 OJ L 306, 23.11.2011, p. 25, ELI: http://data.europa.eu/eli/reg/2011/1176/oj.

Whereas:

(1) The euro area economy has shown resilience in the face of the major economic shocks of recent years, also reflecting a strong, coordinated, and timely policy response, but it has recently lost momentum. After the sizeable recovery in 2021 and 2022, growth in the euro area is expected to slow to 0.6 % in 2023. Although moderating, high consumer prices for most goods and services have been taking a heavy toll on the economy, despite declining energy prices, and external demand is not providing strong support. Meanwhile, the effect of tightening monetary policy works its way through the economy. On the positive side, the labour market remains strong, with the unemployment rate at a record low, with differences across Member States and their regions, and participation and employment rates at a record high, although signs of cooling are emerging. In 2024, a gradual recovery in growth is expected, by 1.2 %, on the back of continued expansion of employment and rising real wages, while inflation will continue to fall. The outlook remains surrounded by high uncertainty and risks, primarily related to the evolution of Russia's ongoing war of aggression against Ukraine, the situation in the Middle East following the brutal and indiscriminate terrorist attacks on Israel by Hamas, which could cause renewed disruptions to energy supplies with a significant impact on energy prices, and the risks related to a structural slowdown in China. Furthermore, the delayed impact of policies to fight against inflation and their possible effects on economic activity may add to the risks surrounding the outlook. Structural changes linked in particular to the intensifying impact of climate change, as illustrated by extreme weather conditions and unprecedented wildfires and floods, also weigh on the outlook.

(2) Following the peak that occurred in October 2022, headline inflation in the euro area has eased, mainly driven by declining energy prices, but also by a gradual broad-based moderation in the other components. Nevertheless, food and services inflation remains high, affecting especially the most vulnerable, and inflationary pressures remain substantial in a number of Member States. Inflation is projected to decline to 3.2 % in 2024, thus remaining above the European Central Bank's (ECB) 2 % target, while falling to 2.2 % in 2025. The disinflation process is aided by the ECB's fastest and largest interest rate increase since the creation of the economic and monetary union (EMU). Sovereign yields in the euro area have increased but spreads have remained relatively stable. The ECB has repeatedly expressed its commitment to keep interest rates high for as long as necessary to bring inflation down to target and clarified that the path of future monetary policy will continue to follow a data-dependent approach.

(3) The energy price shock has dented cost competitiveness in the euro area, in particular for the more energy-intensive Member States and industries. So far, the negative impact of higher costs has been mitigated by exchange rate movements and by temporary measures taken by governments to support businesses and vulnerable households. However, the high cost of energy, together with differences in the energy intensity of the economies of the Member States and with differences in the energy sourcing of the Member States, as well as differences in market structures and policy responses, have contributed to large inflation differentials within the euro area. Despite the decrease in energy prices in 2023, those inflation differentials have only partly subsided so far. Together with the dispersion in wages growth over the past two years, price differentials, if they continue, could result in competitiveness gaps across euro area Member States and contribute to macroeconomic imbalances that could undermine the proper functioning of the euro area. It is therefore important to address all macroeconomic imbalances. In the medium term, the ability of the euro area and of the Member States to strengthen productivity relies, in part, on the capacity to sustain innovation and investment. In that respect, prospects of energy prices and costs that could be permanently higher than those of trading partners, a persistent gap in productivity growth compared to peers, and rising risks of geoeconomic fragmentation would put the euro area economy at a disadvantage.

(4) The current macroeconomic environment, which is characterised by persistent uncertainty, high inflation, and the compromised competitiveness of the euro area, calls for an ambitious policy agenda. In the short term, ensuring the return of inflation to the ECB's 2 % target remains a priority. In addition, persistent differences in inflation rates between Member States could translate into competitiveness divergences. Fiscal policy should avoid adding to inflationary pressures. Real income decreased in 2022, calling for wage developments to mitigate the loss in purchasing power, in particular for low-income earners. At the same time, second-round effects on inflation and competitiveness should be closely monitored by public authorities and taken into account in wage formation. In addition, limiting risks to macro-financial stability and the macroeconomic impact of tighter financial conditions remains crucial. Going forward, the euro area must continue fostering inclusive and sustainable growth and preserve its global competitiveness, while avoiding divergences across the euro area. In this respect, reforms and investments, including reforms and investments to foster the green and digital transitions and the euro area's resilience, are instrumental. The timely and effective involvement of social partners, and strong social dialogue are key to supporting policy design and a broad ownership that fosters implementation.

(5) After a sizeable crisis-related expansion from 2020 to 2022, which helped address the external shocks and protect vulnerable households and viable firms, the overall fiscal stance in the euro area is expected to be restrictive in 2023 and 2024, which is consistent with the need to reduce public deficit and debt levels and the need to avoid fuelling inflationary pressures, while remaining agile in view of the high uncertainty. Between 2020 and 2022, the expansionary euro area fiscal stance, amounting to around 4 % of gross domestic product (GDP), supported the economy in the face of the COVID-19 crisis and the energy price boom following Russia's full-scale military invasion of Ukraine. In 2023 and 2024, the aggregate fiscal stance is expected to turn contractionary, by 0.5 % of GDP in both years, primarily due to the near complete phase out of crisis-related energy measures. The overall contractionary fiscal stance expected in 2023 and 2024 will contribute to restoring fiscal buffers over time and thus to enhancing the sustainability of public finances. Therefore, ensuring compliance with the limits to net expenditure growth recommended by the Council of the European Union (the Council) is key. Besides the need to maintain a prudent fiscal strategy, public investment needs to be maintained and increased as much as possible, where needed, and private investment needs to be further promoted in order to support competitiveness, inclusive and sustainable long-term growth, and fair green and digital transitions.

In 2023 and 2024, public investment is expected to further expand in most Member States, with continuing support of the Recovery and Resilience Facility established by Regulation (EU) 2021/241 of the European Parliament and of the Council[3] (RRF) and other Union funds. Public finances also face pressure arising from high costs in areas such as ageing, defence, as well as the less favourable interest-growth differential. As part of their country-specific recommendations, a number of euro area Member States were recommended to take measures to improve the sustainability of their pension and healthcare systems and to adopt tax reforms. Conducting government spending reviews as a regular part of the annual and multiannual budgetary processes would help improve the efficiency and quality of public expenditure. Government spending reviews need to have a clear scope, mandate and methodology and their outcomes should be communicated clearly to the public. Measures addressing aggressive tax planning, tax avoidance and tax evasion can also make tax systems more efficient and fairer, while supporting recovery and increasing revenues.

[3] Regulation (EU) 2021/241 of the European Parliament and of the Council of 12 February 2021 establishing the Recovery and Resilience Facility (OJ L 57, 18.2.2021, p. 17, ELI: http://data.europa.eu/eli/reg/2021/241/oj).

(6) The aggregate debt-to-GDP ratio of the euro area is expected to decline by a cumulative 2.8 percentage points over 2023-2024, reaching 89.7 % of GDP by the end of 2024. The decline is mainly driven by nominal GDP growth which outpaces the average interest rate paid on outstanding debt. However, debt remains elevated in several Member States and the overall higher interest rates will gradually feed into the higher debt servicing costs, with a negative impact on debt dynamics all other things being equal. In December 2023, the Council reached an agreement on the Economic governance review package consisting of a Regulation of the European Parliament and of the Council on the effective coordination of economic policies and multilateral budgetary surveillance and repealing Council Regulation (EC) No 1466/97, Council Regulation amending Regulation (EC) No 1467/97 on speeding up and clarifying the implementation of the excessive deficit procedure, and Council Directive amending Directive 2011/85/EU on requirements for budgetary frameworks of the Member States. The reform of the economic governance framework aims to promote realistic, sustained and gradual fiscal adjustments guided by country-specific medium-term plans and to enhance sustainable growth by incentivising relevant reforms and investments. The reformed economic governance framework will create more clarity and predictability for fiscal policy going forward, promoting debt sustainability and economic growth at the same time.

(7) The net cost of emergency support measures taken to mitigate the economic and social impact of the rise in energy prices remained high in 2023, albeit slightly declining in the context of falling energy prices from their peak in 2022. The Commission estimates that the net budgetary cost of such emergency support measures amounts to 1.0 % of euro area GDP in 2023, down from 1.3 % in 2022. Even if the targeting has improved, almost half of the related budgetary cost in 2023 has gone towards price measures that are not targeted to vulnerable households and companies. Most of the measures are now expected to be phased out over the course of 2024, in line with the expected stabilisation in energy prices. If such estimates materialise, there will be a residual budgetary cost of around 0.2 % of GDP in 2024 for the euro area as a whole. However, should energy prices increase again to levels that would necessitate new or continued support measures, such support measures should be targeted at protecting vulnerable households and companies, fiscally affordable and should preserve incentives for energy savings. More generally, and beyond crisis-related energy measures, stronger use of environmental taxation, in line with the polluter-pays principle, together with phasing-out of fossil fuel subsidies which do not address energy poverty or just transition, and other environmentally harmful subsidies could contribute to increasing the fiscal space for euro area Member States.

(8) Sustaining a sufficiently high level of high-quality public investment can help mobilise private investment, boost potential growth and competitiveness, and support the green and digital transitions, as well as strengthen social and economic resilience. In this respect, a full implementation of the reforms and investments under the RRF and of the cohesion policy funds is a priority. The implementation of national recovery and resilience plans is well under way, but progress varies across Member States and implementation needs to be stepped up in some instances to bridge accumulated delays. As of mid-November, the Commission has received 34 payment requests from 19 euro area Member States and disbursed a total amount of EUR 162.1 billion in grants and loans. This breaks down into EUR 51.6 billion paid in pre-financing and EUR 110.5 billion disbursed after milestones and targets were reached. The pace of disbursement in 2023 has been somewhat slower than expected, partly because Member States are focusing on revising their national recovery and resilience plans due to changes in the grant allocation, new loan requests and the introduction of REPowerEU chapters. Since the beginning of the COVID-19 crisis, cohesion policy, under the European Regional Development Fund, Cohesion Fund, European Social Fund and the Youth Employment Initiative, has disbursed close to EUR 120 billion to euro area Member States. In the context of the mid-term review of the cohesion policy, Member States will have the opportunity to review cohesion policy programmes and allocate funds to address pressing needs and emerging challenges. The 2024 European Semester cycle will provide orientations for the mid-term review and help direct funding in light of the socio-economic context and challenges in the Member States and their regions, while continuing to promote complementarity with the RRF and other Union funds.

(9) Promoting private investment, innovation and skills development is key to enhancing productivity and strengthening the competitiveness of the euro area, in particular in support of the green and digital transitions. Removing barriers to investment, including through reforms that streamline and digitise planning, permitting and other administrative procedures, would help boost private investment. Industrial policy and supply-side-oriented policies can also contribute by supporting investment, safeguarding competitiveness, and avoiding risks linked to excessive reliance on a limited number of third countries for key technologies, raw materials and industrial inputs. As part of its Green Deal Industrial Plan for the Net-Zero Age, the Commission has put forward several initiatives to strengthen strategic sectors, including the Proposal for a Regulation of the European Parliament and of the Council on establishing a framework of measures for strengthening Europe's net-zero technology products manufacturing ecosystem (Net-Zero Industry Act), the Proposal for a Regulation of the European Parliament and of the Council establishing a framework for ensuring a secure and sustainable supply of critical raw materials and amending Regulations (EU) 168/2013, (EU) 2018/858, 2018/1724 and (EU) 2019/1020, and the Proposal for a Regulation of the European Parliament and of the Council establishing the Strategic Technologies for Europe Platform ('STEP') and amending Directive 2003/87/EC, Regulations (EU) 2021/1058, (EU) 2021/1056, (EU) 2021/1057, (EU) No 1303/2013, (EU) No 223/2014, (EU) 2021/1060, (EU) 2021/523, (EU) 2021/695, (EU) 2021/697 and (EU) 2021/241 (the STEP proposal). The Innovation Fund and the Modernisation Fund also provide financial support for the necessary transition in the private sector. In addition, through the adoption of the Temporary Crisis and Transition Framework for State Aid measures to support the economy following the aggression against Ukraine by Russia, the Commission has enabled Member States to use the flexibility foreseen under State aid rules to support measures in sectors which are key for the transition to a climate-neutral economy.

While euro area Member States have taken measures to support sectors that are most exposed to the energy crisis and to support the green transition, such measures are generally decided at national level, entailing a risk of distortion of the level playing field in the internal market. The STEP proposal aims to address the heightened need for Union public investments in strategic technologies, to leverage much greater private investments and can help safeguard cohesion and the internal market. Strong capital markets are crucial for an inclusive, competitive, and resilient euro area economy. A deeper capital markets union (CMU) would help mobilise the required private financing for the green and digital transitions, reduce fragmentation and improve access to finance. In February 2023, the European Council called on the Council and the European Parliament to speed up the implementation of the CMU action plan by advancing and finalising work on the legislative proposals in that area. In May 2023, the Eurogroup has set the aim to reach an agreement by March 2024 on areas that the Commission should consider to further deepen the CMU. As part of the work on the EMU, the Commission tabled a package of proposals in 2023 on a legal framework for a digital euro consisting of the Proposal for a Regulation of the European Parliament and of the Council on the legal tender of euro banknotes and coins, the Proposal for a Regulation of the European Parliament and of the Council on the provision of digital euro services by payment services providers incorporated in Member States whose currency is not the euro and amending Regulation (EU) 2021/1230 of the European Parliament and the Council, and the Proposal for a Regulation of the European Parliament and of the Council on the establishment of the digital euro. A digital euro, which would complement cash denominated in euro, would support the digitalisation of the economy as well as innovation in retail payments while reducing payments fragmentation across the Union. If issued, the digital euro would introduce a new possibility for using risk-free central bank money in European payment services. It would also facilitate cross-border payments and contribute to strengthening the international role of the euro as well as Union’s open strategic autonomy.

(10) Despite a decelerating growth impetus, the labour market remains resilient. Employment continued to grow in 2023, together with working hours, against the backdrop of labour and skills shortages as well as an increased tendency of labour hoarding by companies. Although the overall good performance has been broad-based across Member States, some groups continue to be under-represented in the labour market, including women, youth and low-skilled persons with disabilities. Active labour market policies, together with the provision of quality and affordable early childhood education and care, as well as long-term care, play a key role in boosting participation and supporting skills provision and acquisition, including for the green and the digital transitions, with a positive impact on potential output growth and competitiveness in the long term. Promoting better working conditions and complementing the harnessing of talents within the Union, managing legal migration from third countries, and ensuring respect for and the enforcement of labour and social rights can help address skills and labour shortages. Euro area Member States issued 664 000 first-work permits to third-country nationals for employment purposes in 2022, a number that almost tripled over the preceding 10 years.

(11) Nominal wages increased in 2022 (+4.8 %) and during the first months of 2023, on the back of high inflation and tight labour markets. While this has partially mitigated losses in purchasing power, nominal wage growth has not kept up with inflation (-3.7 % for real wages in 2022). Nominal wage growth is likely to be strong over 2023 and 2024, while real wages are set to increase moderately, strengthening domestic demand. At the same time, the expected growth in wages may affect prices of goods with a strong domestic labour component, such as services, although the impact on prices could be cushioned if past increases in unit profits are unwound. Higher wages, if not matched by productivity gains, could also affect competitiveness and durable divergences across the euro area may, among other factors, lead to macroeconomic imbalances. Therefore, in accordance with national practices and respecting the role of social partners, wage agreements should appropriately reflect developments in the euro area in addition to sectoral and national dynamics.

(12) The rise in the cost of living, mainly related to the energy crisis and the associated worsening in the terms of trade, has had a negative impact on real incomes as well as significant social implications. In 2022, prices grew by 17.5 % for housing, water, electricity, gas and other fuels, by 10.5 % for food and non-alcoholic beverages and by 11.2 % for transport. Low-income households suffered from particularly large cost-of-living adjustments. Over half of euro area Member States witnessed increases in material and social deprivation as well as in energy poverty, in spite of nominal wage developments and support mechanisms. In several Member States, increases in the cost of living disproportionately affected older people and people living in rural areas.

(13) The euro area banking sector has proven to be resilient despite various episodes of heightened market turmoil. The euro area banking sector is now well capitalised and profitable, as confirmed by the Union-wide 2023 stress tests performed by the European Banking Authority established by Regulation (EU) No 1093/2010 of the European Parliament and of the Council[4]. Alongside monetary and lending standards tightening, credit flows to the private sector are slowing down markedly. Going forward, there is a risk of weaker asset quality if the macroeconomic outlook deteriorates sharply, together with interest rates staying high for an extended period of time. At the same time, the non-bank financial intermediation sector may be confronted with vulnerabilities. In a context of tighter financing conditions, monitoring risks in a timely manner, proactively engaging with debtors and actively managing non-performing loans will be important to maintaining the financial sector's ability to finance the economy. Other risks to financial markets may emerge. In particular, higher risk premia amid tightening liquidity conditions may lead to a stronger and potentially disorderly correction in asset prices. The ongoing adjustment in the residential and commercial real estate markets also needs to be closely monitored. Rising interest rates and a worsening debt-servicing capacity may lead to substantial corrections in real estate prices and could spur financial instability.

4 Regulation (EU) No 1093/2010 of the European Parliament and of the Council of 24 November 2010 establishing a European Supervisory Authority (European Banking Authority), amending Decision No 716/2009/EC and repealing Commission Decision 2009/78/EC (OJ L 331, 15.12.2010, p. 12, ELI: http://data.europa.eu/eli/reg/2010/1093/oj).

(14) In the Statement of the Euro Summit of March 2023 euro area leaders reiterated their commitment to complete the banking union in line with the statement of the Eurogroup of 16 June 2022. Against this background, in April 2023, the Commission tabled a proposal on the reform of the bank crisis management and deposit insurance framework. That proposal aims at building a framework suited for failing banks of any size and business model, including smaller players, and in this way preserving financial stability, minimising the use of public funds and strengthening depositor confidence. The Eurogroup committed to subsequently review the state of the banking union and identify, in a consensual manner, possible further measures regarding the other outstanding elements to strengthen and complete the banking union. In addition, the ratification of the revised Treaty establishing the European Stability Mechanism, allowing for the introduction of the common backstop to the Single Resolution Fund established by Regulation (EU) No 806/2014 of the European Parliament and of the Council[5] would further strengthen the resilience of the euro area,

HEREBY RECOMMENDS that euro area Member States take action, individually, including through the implementation of their national recovery and resilience plans, and collectively within the Eurogroup, in the period 2024–2025 to:

[5] Regulation (EU) No 806/2014 of the European Parliament and of the Council of 15 July 2014 establishing uniform rules and a uniform procedure for the resolution of credit institutions and certain investment firms in the framework of a Single Resolution Mechanism and a Single Resolution Fund and amending Regulation (EU) No 1093/2010 (OJ L 225, 30.7.2014, p. 1, ELI: http://data.europa.eu/eli/reg/2014/806/oj).

1. Adopt coordinated and prudent fiscal policies to keep debt at prudent levels or put debt ratios on a plausibly downward path. While policies should remain agile in view of the prevailing uncertainty, achieve an overall restrictive fiscal stance in the euro area in line with the Council country-specific recommendations, and thus enhance the sustainability of public finances and avoid fuelling inflationary pressures. Wind down energy-related emergency support measures as soon as possible in 2024 and use the related savings to reduce deficits. Develop fiscal strategies to achieve a prudent medium-term fiscal position and strengthen debt sustainability where necessary, through determined, differentiated, gradual and realistic consolidation, combined with high-quality public investments and reforms, notably to deliver higher sustainable growth and boost the resilience of the euro area in the face of future challenges. Where needed, include in such strategies measures to further increase the efficiency and quality of public expenditure and to improve the sustainability and adequacy of the pension, healthcare and long-term care systems.

2. Sustain a high level of public investment, to support the green and digital transitions, strengthen productivity, competitiveness and boost economic and social resilience. Ensure the continued, swift and effective implementation of the national recovery and resilience plans, including their REPowerEU chapters. Make full use of cohesion policy programmes and ensure that the mid-term review of cohesion policy programmes takes into account, inter alia, the new challenges and recommendations identified in the European Semester and the progress in implementing the European Pillar of Social Rights, without reducing their overall ambition.

3. In accordance with national practices and respecting the role of social partners, support wage developments that mitigate loss of purchasing-power, especially for low-income earners, taking due account of risks to inflation and competitiveness dynamics, as well as avoiding lasting divergences within the euro area. Promote upskilling and reskilling, including for the green and the digital transitions. Implement active labour market policies to address labour and skill shortages and increase productivity and growth. Promote better working conditions to attract and retain workers in order to address labour shortages. Take measures to facilitate managed legal migration of third-country workers in occupations experiencing labour shortages, in full complementarity to the harnessing of talents from within the Union. Safeguard and strengthen adequate and sustainable social protection and inclusion systems. Ensure the effective involvement of social partners in policymaking and strengthen social dialogue.

4. Remove investment obstacles to reduce the prevailing gap in investment for the green and digital transitions. Improve access to finance, in particular for innovative companies and small and medium-sized enterprises, through further progress in deepening and strengthening the capital markets union. Ensure that public support to relevant strategic sectors is targeted, with no distortions of the level playing field in the internal market and with a view to enhancing the competitiveness of the euro area and the Union's open strategic autonomy. Continue strengthening the international role of the euro and make further progress in the work on the digital euro.

5. Preserve macro-financial stability, maintain the credit channels to the economy and avoid the risk of financial fragmentation. Monitor risks linked to tighter financial conditions, in particular risks that are related to asset quality and to potential corrections in asset prices, including in real estate markets. Monitor developments in the banking sector and non-bank financial intermediation to prevent the build-up of systemic risk and negative spillovers to the economy. Complete the banking union by continuing to work on all outstanding elements.

6. Further steps in deepening the economic and monetary union (EMU) should take into account the lessons learnt from the design and implementation of the Union's comprehensive economic policy response to the COVID-19 crisis. Progress in deepening the EMU should be continued in full respect of the Union's internal market and in an open and transparent manner towards non-euro area Member States.

Done at …,

For the Council
The President