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NOTE

From:	General Secretariat of the Council
To:	Delegations
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Subject:	Recommendation for a COUNCIL RECOMMENDATION on the economic policy of the euro area

Delegations will find here attached the Eurogroup version agreed on 16 December 2020 of the draft Council recommendation on the economic policy of the euro area. Following the January's ECOFIN VC, the text is to be approved at the first available physical Council meeting or by written procedure.

The formal adoption of the text should take place after the endorsement by the European Council in March 2021.

Recommendation for a

COUNCIL RECOMMENDATION

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,

1 OJ L 209, 2.8.1997, p. 1.
2 OJ L 306, 23.11.2011, p. 25.

Whereas:

(1) As a result of the COVID-19 pandemic, the euro area economy experienced a sudden and deep recession in the first half of 2020. Notwistanding the strong rebound in the third quarter of 2020, accompanying the lifting of containment measures, the pick-up in the spread of Covid-19 and the new containement measures in the fourth quarter have further increased uncertainty and showed that the euro area remains vulnerable to the persisting health crisis. The COVID-19 crisis has produced a series of large demand and supply side shocks translating into an expected decline of GDP by 7.8% in 2020, according to the Commission services' autumn 2020 economic forecast. The recovery in 2021 is accordingly projected to be slower than previously expected and a large output gap of some -7.0% of potential euro area GDP in 2020 is not projected to close by the end of 2021. Considerable uncertainty prevails over the economic outlook, related to the evolution of the pandemic and behavioural changes by economic agents. Prompt action at the national and Union level, including the agreement reached by the European Council on the Next Generation EU (NGEU) package, has decisively helped to offset some of the negative consequences of the shock and stabilise markets. Both private consumption and investment took a severe hit, affecting in turn negatively prices and wages. The labour market outlook has also taken a turn for the worse, interrupting seven years of improvements. The increase in unemployment has so far been mitigated by successful implementation of ambitious policy measures in all Member States – such as short-time work schemes and other support policies to avoid mass lay-offs and large income losses – and the related drop in total hours worked as well as by a decline in activity rates.

(2) The COVID-19 crisis is increasing the economic divergences across euro area Member States. Several factors are driving these divergences, including: the intensity and duration of the COVID-19 shock; the relative size and economic importance of contact intensive sectors (e.g. tourism, business travel and hospitality) and the differences in fiscal space available. These differences impact confidence, investments and growth prospects as well as regional disparities that pre-existed the crisis but now may be exacerbated. Over the longer-term, the current COVID-19 crisis risks having permanent negative effects on potential growth and income gaps due to lower human and physical capital (both tangible and intangible). That could translate into even lower growth in labour productivity and incomes and higher inequality.

(3) The fast and forceful reaction by the Union, including Next Generation EU (NGEU), which comprises the Recovery and Resilience Facility (RRF), has boosted market confidence and shown the solidarity and unity of purpose of Member States in coordinating their efforts to restart economic growth and strengthen economic and social resilience. A number of new instruments for the Union and the euro area were agreed in a very short space of time. These instruments already provide a safety net for workers (through the European Instrument for Temporary Support to mitigate Unemployment Risks in an Emergency - SURE)[3], for businesses (through a scheme by the European Investment Bank) and for Member States to support domestic financing of direct and indirect healthcare, cure and prevention related costs due to the COVID 19 crisis, through the European Stability Mechanism's Pandemic Crisis Support Instrument.[4] The Union policy response also included the activation of the general escape clause of the Stability and Growth Pact and a temporary framework to use the flexibility under EU state aid rules.[5] The cohesion policy funds were redirected where most needed through the Coronavirus Response Investment Initiative Plus (CRII and CRII+).[6]

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3 OJ L 159, 20.5.2020, p. 1–7.

4 https://www.consilium.europa.eu/media/44011/20200508-pcs-term-sheet-final.pdf

5 OJ C 91I, 20.3.2020, p. 1–9, OJ C 112I, 4.4.2020, p. 1–9, OJ C 164, 13.5.2020, p. 3–15, OJ C 218, 2.7.2020, p. 3–8.

6 OJ L 99, 31.3.2020, p. 5–8.

(4) The implementation of well-designed policies in the context of NGEU and its main instrument, the RRF, will provide a new momentum to Member States for embarking on growth-enhancing reforms and increase the level and quality of investments, consistent with serving the objectives of resilience and the green and digital transitions. It should help build human capital, support workers' successful job transitions which, alongside the cohesion policy funds, will be essential to ensure cohesion, foster employment and productivity, and enhance economic and social resilience. EU growth objectives, and national structural challenges, including those identified in the 2019 and 2020 country-specific recommendations, are key. The Annual Sustainable Growth Strategy 2021 (ASGS[7]), which promotes these objectives, puts forward seven flagship initiatives: (1) Power up, (2) Renovate, (3) Recharge and Refuel, (4) Connect, (5) Modernise, (6) Scale-up, (7) Reskill and upskill. Those flagships areas represent common challenges that call for coordinated investments and reforms. Member States are encouraged to channel investments, implement reforms and integrate further their value chains in these flagship areas. The proposed Recovery and Resilience Facility Regulation provides, among others, that euro area Member States' Recovery and Resilience Plans shall be consistent with the challenges and priorities identified in the Council recommendation on the economic policy of the euro area. This consistency should be taken into account in the assessment of the Recovery and Resilience Plans.

(5) The euro area requires a mix of economic policies that is supportive, coordinated, comprehensive and consistent to cushion the impact of the COVID-19 pandemic, in full compliance with the Treaty safeguards concerning the respective institutions. The aim is to limit any negative long-term impact on the labour market, to reduce significant economic and social divergences, to address imbalances and other macro-significant risks and, more broadly, to avoid negative consequences for potential growth and price stability and to ensure sustainable public finances over the medium term. The mutual consistency of the three core dimensions of the euro area policy mix – monetary, fiscal and structural – along with financial stability, is essential to ensure a supportive aggregate policy stance for the euro area.

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7 COM(2020) 575 final.

(6) The timely European Central Bank (ECB) monetary policy interventions aim at keeping the monetary transmission channels intact and safeguarding medium-term price stability. The ECB announced substantial purchases of public and private sector assets under its Pandemic Emergency Purchase Programme (PEPP, EUR 1850 billion until at least end of March 2022)[8] and under the Asset Purchase Programme (APP, net purchases of EUR 20 billion per month, together with an additional envelope of EUR 120 billion until the end of 2020)[9]. Moreover, the ECB offers Targeted Longer-Term Refinancing Operations at very favourable conditions, supporting bank lending to firms and households.

(7) The fiscal stance is forecast to be highly expansionary in 2020 and to remain supportive in 2021 at both euro area and national level, excluding emergency measures and also thanks to some recovery measures already announced. Coordination of national fiscal policies, in full respect of the Stability and Growth Pact, is crucial for the effective response to the COVID-19 shock, a sustainable recovery, and the proper functioning of the Economic and Monetary Union (EMU). On 20 March 2020, the Commission concluded that the EU economy was experiencing a severe economic downturn and the conditions to activate the general escape clause of the Stability and Growth Pact were met. This conclusion was endorsed by the finance ministers of the Member States.[10] Member States introduced sizeable budgetary measures to contain the pandemic and provide support to individuals and businesses particularly affected, as well as exceptional liquidity support, mainly via guarantees provided to companies and to banks to ensure the flow of credit. Further coordinated fiscal support will be provided at the EU level, notably through the RRF, and the general escape clause will remain active in 2021. In spring 2021, taking into account updated macroeconomic projections, the Commission will reassess the situation and take stock of the application of the general escape clause.

8 OJ L 91, 25.3.2020, p. 1–4.
9 OJ L 157, 15.6.2016, p. 28–32.
10 https://www.consilium.europa.eu/en/press/press-releases/2020/03/23/statement-of-eu-ministers-of-finance-on-the-stability-and-growth-pact-in-light-of-the-covid-19-crisis/

(8) The economic fallout from COVID-19 is having a large negative impact on public finances. When health and economic conditions allow, a refocusing of fiscal policies towards achieving prudent medium-term fiscal positions, including by phasing out emergency measures, will contribute to ensuring fiscal sustainability in the medium term. This should be done in a way that mitigates the social and labour-market impact of the crisis and contributes to social sustainability. Reforms aimed at improving the composition of national budgets and at ensuring fiscal sustainability over the longer term, including in view of climate change and health challenges, appear particularly relevant. Improving the composition of national budgets, especially through spending reviews and effective public procurement frameworks, can create much-needed fiscal space. Green budgeting practices can also help address the challenges of climate mitigation and adaptation, and environmental protection. Adequate, efficient and inclusive health and social protection systems offer much-needed protection to those in need, play a key role as automatic stabilisers and should preserve fiscal sustainability. Similarly, reforms that strengthen the functioning of labour, capital, products and services markets – through appropriate implementation and sequencing – increase potential output, while avoiding a negative short-term impact on aggregate demand.

(9) The COVID-19 crisis is reinforcing the importance of reforms for more efficient and fairer public revenue systems. As the tax wedge on labour in the majority of euro area Member States remains high, these reforms include shifting the tax burden towards tax bases that are less detrimental to labour supply and demand, productivity, investment and growth, while taking into account the related distributional impact. An increased use of environmental taxation and/or other forms of pricing of externalities can contribute to sustainable growth by incentivising “greener” behaviours. Measures addressing aggressive tax planning and tax avoidance, both internationally and in the Union, can make tax systems more efficient and fairer. Moreover, globalisation has made it necessary to adjust the taxation framework to fit a modern and increasingly digitalised economy, both at global and at EU level. Work is ongoing within the OECD framework to reach a global-consensus based solution to address tax challenges arising from the digitalisation of the economy.

(10) Frontloading reforms that tackle investment bottlenecks and supply-side constraints is of particular relevance considering the high level of uncertainty brought by the COVID-19 shock and its detrimental effect on investment. Measures that accelerate the absorption of EU funds and an effective and efficient utilisation of resources are essential, in particular in Member States lagging behind in these areas and where EU funds finance a significant share of investments. Reforms that reduce the administrative burden for firms (e.g. digitalisation of public administrations, including electronic identification, judicial reforms) and prevent the misuse of funds (e.g. corruption, fraud and anti-money laundering[11]) can improve the business environment and help boost private investment, job and firm creation.

[11] Communication C(2020) 2800 final from the Commission of May 20 on an Action Plan for a comprehensive Union policy on preventing money terrorist financing.

(11) The COVID-19 crisis has led to substantial revenue losses for many firms and poses risks to corporate solvency across the euro area. Effective insolvency frameworks play a crucial role in supporting viable firms undergoing temporary problems and providing for the orderly exit of non-viable firms. Improving insolvency frameworks can also help address the likely increase in non-performing loans and maintain credit to the economy by facilitating the cleaning up of bank balance sheets and spur cross-border investment over the longer term. In this context, the Restructuring and Second Chance Directive (2019/1023)[12] was adopted to introduce minimum standards across Member States in the national solvency legislation in order to ensure that preventive restructuring frameworks are available to debtors in financial difficulty, to provide procedures leading to a discharge of debts incurred by over-indebted entrepreneurs, and to increase the efficiency of all types of insolvency procedures. It is important to proceed with the transposition and the implementation of the directive. The European Commission also announced in the Capital Markets Union action plan of September 2020[13] work towards minimum harmonisation or increased convergence in targeted areas of core non-bank insolvency. Beyond this, there is scope for Member States to further assess the efficiency and effectiveness of their insolvency frameworks in line with international best practices and address the remaining deficiencies.[14]

12 OJ L 172, 26.6.2019, p.18-55.
13 COM(2020) 590 final.
14 The Eurogroup identified a number of principles including early identification of debt distress and availability of early restructuring procedures. See https://www.consilium.europa.eu/en/meetings/eurogroup/2016/04/22/.

(12) Further deepening the single market in goods and services, and adapting the euro area to the digital era, can be a major engine of growth, convergence and resilience. The common currency and the single market have been working in tandem to create better conditions for economic stabilisation and long-term growth. The COVID-19 crisis has boosted the use of digital tools, highlighted the importance of the digital single market and has accelerated the use of digital and cashless payment methods. However, the single market remains incomplete, especially in the area of services and more specifically in retail trade and professional services. The single market has the potential to limit price rigidities, thereby benefitting monetary policy transmission and economic resilience. The single market also helps with the mobility of production factors, which allows sectors, regions and Member States to minimise economic costs (e.g. unemployment) in response to shocks. To achieve further integration of the single market for goods and services, it is necessary to remove all remaining unnecessary restrictions, enhance market surveillance mechanisms and take measures to guarantee the administrative capacity in order to achieve these objectives.

(13) Reforms and investment that improve labour market integration and transitions, with a particular attention to digital and green jobs, are essential to increase economic and social resilience and support the recovery. The immediate national and Union crisis measures limited the negative economic and social impact on workers. At the same time, a number of long-standing reforms have become even more urgent now: effective active labour market policies, including individualised support, improving the quality and inclusiveness of education and training systems to strenghen educational outcomes from an early age, strong re- and up-skilling measures and investment in adult education and training and in online learning platforms, addressing skills shortages, increasing the employment prospects of the most vulnerable segments of the working population, including the young and long-term unemployed, as well as closing the gender gaps. Fostering quality job creation, and improving working conditions, notably by ensuring adequate minimum wages and addressing labour market segmentation and barriers to labour mobility, are key to support a sustainable and inclusive recovery. Social dialogue and collective bargaining play an important role in the successful design and implementation of policies.

(14) Access to adequate, inclusive and sustainable health and social protection systems, which function as automatic stabilisers in the crisis, is important for economic and social resilience. These help to maintain social cohesion, decent living standards and good population health, which is fundamental to a productive labour economy, through the entire economic cycle and address poverty and social exclusion. Investments to support health reforms and resilient health systems need to remain a priority for Member States. The implementation of the European Pillar of Social Rights[15] is key to guide policies. In the face of the crisis, the need to ensure adequate social protection coverage for all, both in terms of quality health- and long-term care, as well as in terms of income replacement for all workers, including those under atypical contracts and the self-employed, has become even more important. Many Member States have adopted temporary income support and social assistance measures in favour of vulnerable groups with very low incomes and workers not entitled to unemployment benefits. Measures have been taken with regard to benefits, eligibility conditions and additional in-kind services. Strengthening of the adequacy and coverage of social protection systems needs to be done in a way that ensures the long-term sustainability of public finances and intergenerational fairness.

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15 Interinstitutional Proclamation on the European Pillar of Social Rights OJ C 428, 13.12.2017, p.10-15.

(15) Significant progress has been achieved in recent years, but the economic fallout from the pandemic has put renewed pressure on the financial sector. Euro area banks entered the current crisis with stronger loss-absorption capacities compared to before the onset of the global financial crisis. Combined with monetary and fiscal policy measures, this has avoided a tightening of market financing conditions, beyond the initial phase of the crisis, and ensured the continued credit provision to the private sector. The crisis is likely to put further pressure on banks' already low profitability levels and non-performing loan ratios. The development of secondary markets for non-performing loans, an efficient deployment of national Asset Management Companies (AMCs), where appropriate, and reforming insolvency frameworks, are particularly important to make progress in this area, along with addressing structural issues of low profitability. These developments could hamper the provision of credit to the economy, which is essential for the recovery. The swift and sizeable policy interventions have supported confidence and helped to preserve macro-financial stability. Government loan guarantee schemes help sustain credit to the economy, protect companies and mitigate feedback loops with the banking sector, but also constitute contingent liabilities for Member States' budgets. Prolongation of insolvency moratoria and forbearance of non-performing loans entails striking a difficult balance between ensuring continued support to viable firms and risking misallocation of funds, increased the losses under an eventual bankruptcy and reduced clarity as to underlying credit quality.

(16) The completion of the EMU architecture remains essential. Filling the remaining gaps could further increase the euro area's stability and resilience and would consequently strengthen the international role of the euro, which has remained broadly stable in recent years. Further steps should take into account the lessons learnt from Europe's comprehensive economic policy response to the COVID-19 pandemic. Beyond its short-term stabilisating effect and its role in supporting the recovery, Next Generation EU has the potential to impact the EMU in the longer term through stimulating growth-enhancing investments and structural reforms and increasing the euro area's resilience to future shocks. The sizeable issuance of euro-denominated debt, including green and social bonds, will add depth and liquidity to the market for high-quality euro-denominated debt securities, and can contribute to strengthening the international role of the euro. Nonetheless, important elements are still missing in EMU, such as a complete Banking Union and a deepened Capital Markets Union. Strengthening the Banking Union remains crucial. This calls for continuing to work, without delay, and with the same level of ambition, on all elements, including those discussed in the High Level Working Group on EDIS, on a consensual basis. Proceeding with the ESM package of reforms and, given the progress made in risk reduction and the further measures outlined in the Eurogroup statement of 30 November 2020, advancing the entry into force of the common backstop for the Single Resolution Fund, by the beginning of 2022, marks another important step towards completing the Banking Union and strengthening EMU. There should be further work on solutions for overcoming limitations in the current set-up for liquidity provision in resolution. Deepening the Capital Markets Union is a key priority, as demonstrated by the new action plan of September 2020. A strong and resilient EMU will also be important to strengthen the international role of the euro and ensure the Union's economic and financial autonomy on which the Commission will put forward a communication, while fully respecting the Union's internal market and pursued in an open and transparent manner towards non-euro area Member States.

HEREBY RECOMMENDS that euro area Member States take action, individually, including through their Recovery and Resilience Plans, and collectively within the Eurogroup, in the period 2021–2022 to:

1. Ensuring a policy stance which supports the recovery

As the health emergency persists, fiscal policies should remain supportive in all euro area Member States throughout 2021.

Policy measures should be tailored to country-specific circumstances and be timely, temporary and targeted. Member States should continue coordinating actions to effectively address the pandemic, sustain the economy and support a sustainable recovery.

When the epidemiological and economic conditions allow, phase out emergency measures while combatting the social and labour-market impact of the crisis. Pursue fiscal policies aimed at achieving prudent medium-term fiscal positions and ensuring debt sustainability, while enhancing investment.

Member States should pursue reforms that strengthen the coverage, adequacy, and sustainability of health and social protection systems for all.

Member States should pay particular attention to the quality of budgetary measures. Improve public procurement frameworks and public financial management, including notably investment frameworks and making use of green budgeting tools. Make use of spending reviews to better focus public expenditure on recovery and resilience needs.

2. Further improving convergence, resilience and sustainable and inclusive growth

Mitigate the risk of further divergences, and enhance economic and social resilience in the euro area by continuing to tackle structural challenges and by implementing reforms that strengthen productivity and employment, ensure a smooth re-allocation of resources and improve the functioning of markets and public administration, and by increasing the level of public investment as well as fostering private investment to support a fair and inclusive recovery consistent with green and digital transitions.

Further integrate the single market for goods and services, including digital, by removing unnecessary restrictions, enhancing market surveillance and guaranteeing sufficient administrative capacity.

Ensure effective active labour market policies and support to job transitions, notably towards the green and digital economy. Foster fair working conditions and address labour market segmentation and strengthen inclusion. Ensure the effective involvement of social partners in policy making, strengthen social dialogue and collective bargaining. Strengthen inclusive education and training systems and investment in skills, addressing skills shortages.

Continue working within the framework of the Council on a global consensus-based solution to address the tax challenges arising from the digitalisation of the economy within the OECD Inclusive framework on Base Erosion and Profit Shifting, with the expectation that agreement will be reached by mid-2021 in that forum. Engage in the relevant preparatory work on the way forward in order to address those tax challenges of the digital economy, including in the absence of an international consensus by mid-2021. Make further progress to combat Aggressive Tax Planning, lower the tax wedge and support a shift towards carbon pricing and environmental taxation.

3. Strengthening national institutional frameworks

Pursue and frontload reforms to address bottlenecks to investments and to ensure the efficient and timely use of EU funds, including of the Recovery and Resilience Facility. Strengthen the effectiveness and digitalisation of public administration, including justice and health systems, as well as public employment services. Reduce the administrative burden for firms and improve the business environment. Continue to improve the frameworks to counter fraud, corruption, and to prevent money laundering and terrorism financing.

Promote concrete actions to increase the efficiency, effectiveness and proportionality of insolvency frameworks, to work out non-performing exposures and ensure an efficient allocation of capital.

4. Ensuring macro-financial stability

Maintain the credit channels to the economy and measures to support viable companies as long as necessary during the emergency of the unprecedented crisis.

Keep sound bank sector balance sheets, including by continuing to address non-performing loans, amongst others through the development of secondary markets for non-performing loans.

5. Completing the EMU and strengthening the international role of the euro

Make progress on deepening the Economic and Monetary Union to increase the resilience of the euro area by completing the Banking Union, by continuing to work, without delay, and with the same level of ambition, on all elements, including those discussed in the High Level Working Group on EDIS, and by deepening the Capital Markets Union, as well as through support for initiatives implementing digital finance, retail finance and sustainable finance policies.Work further on solutions for overcoming limitations in the current set-up for liquidity provision in resolution and on strengthening the European regulatory and supervisory framework, including by ensuring consistent and effective supervision and enforcement of anti-money laundering rules.

Further steps in deepening the Economic and Monetary Union should take into account the lessons learnt from Europe's comprehensive economic policy response to the COVID-19 pandemic. Progress, in full respect of the Union's internal market and pursued in an open and transparent manner towards non-euro area Member States, will contribute to enhancing the international role of the euro and promote Europe's economic interests globally.

Done at Brussels,

For the Council
The President