Box 3

THE 2008 UPDATE OF THE INTEGRATED POLICY GUIDELINES OF THE LISBON STRATEGY

In March 2008 the European Council launched the 2008-10 cycle of the Lisbon strategy for growth and jobs. Among other objectives, the Lisbon strategy aims to increase economic growth, productivity and labour utilisation in the European economy.

The Lisbon strategy was renewed in spring 2005 when the European Council endorsed a new governance framework. At the core of this new framework are the Integrated Guidelines for Growth and Jobs which cover a three-year policy cycle and bring together the Broad Economic Policy Guidelines and the Employment Guidelines.[1] Reviewing the results at the end of the 2005-08 cycle, the European Council concluded at its meeting in March 2008 that the Lisbon strategy is starting to deliver results and confirmed that the current Integrated Guidelines continue to provide the right framework for economic policies aimed at enhancing growth and employment in Europe. Therefore, the Integrated Guidelines remain unchanged and the focus for the new cycle (2008-10) should be on the implementation and delivery of reforms.[2] As regards the euro area, the Council noted that further significant reform efforts are still required to prepare countries for the challenges of globalisation, strengthen the foundations for economic success and ensure the smooth functioning of Economic and Monetary Union. The recommendations for euro area countries include: pursuing their medium-term budgetary consolidation objectives in line with the Stability and Growth Pact, improving the quality of public finances by reviewing public expenditure and taxation, increasing competition, especially in services, and improving the flexibility and security of labour markets. This box reviews the progress made in the implementation of the guidelines, as well as the recommendations for the new 2008-10 cycle.

Progress with economic policy reforms

Economic conditions have been favourable since 2005 when the Lisbon strategy for growth and jobs was relaunched. This can be seen in an average annual euro area GDP growth rate of 2.4% for the period 2005-07 and a fall in the unemployment rate from 8.8% in 2005 to 7.4% in 2007. While the favourable labour market developments mainly reflect cyclical effects, there is also some evidence of a structural component linked to past reforms enacted by euro area countries.

Progress in implementing structural reforms is evident in higher levels of employment, in particular among women and older people. Furthermore, a number of euro area countries have been successful in implementing measures to increase competition in some areas of the services sector and some have cut the administrative burden and put in place measures to facilitate starting a business.

1 See the box entitled "The Integrated Guidelines for Growth and Jobs 2005-2008" in the August 2005 issue of the Monthly Bulletin.
2 See "Integrated Guidelines for Growth and Jobs (2008-2010) including a draft for a Council recommendation on the broad guidelines for the economic policies of the Member States and the Community" in the 28 February 2008 draft report from the ECOFIN Council to the European Council on the Broad Economic Policy Guidelines 2008-2010.

Regarding public finances, several countries have made significant progress on moving to sound budgetary positions. Moreover, some countries have reported measures intended to both reduce public expenditure and improve its composition, while others have announced revenue measures focused on reducing the distortions arising from the tax system and administrative charges.

Continuing challenges

While these achievements are encouraging, euro area countries still suffer from structural weaknesses that hamper labour supply, job creation, innovation and the adoption of technological advances and limit their capacity to respond to economic shocks.

In recent years productivity growth has remained weak, constraining general income growth. A sustained improvement in productivity growth therefore remains a key challenge for economic policies in the euro area.[3] This holds true in particular in several services sectors where productivity growth has stalled. Over the period 1995-2005, compared with the previous 15 years, euro area labour productivity growth fell in most non-information and communications technology-related sectors and especially in market services, including distribution and financial and business services, whereas it significantly accelerated in the United States and other countries. It is therefore imperative that euro area countries implement measures to enhance competition, including across countries. This can be achieved by reducing rigidities in product markets, in particular energy markets, and by the implementation of the Services Directive in its entirety.[4] Further product and services market reforms aimed at increased cross-border competition and further integration of markets across the euro area countries would strengthen incentives for firms to eliminate inefficiencies, improve their performance and innovate. This would increase their capacity to smoothly and quickly adjust to economic shocks.[5] It would also provide incentives to increase research and development spending, which in 2006 averaged less than 2% of GDP in the euro area countries and is very likely to fall short of the Lisbon target of reaching 3% of GDP by 2010. Efforts to improve the business environment have sometimes been implemented in a piecemeal way as opposed to being part of an integrated approach geared towards encouraging entrepreneurship, in particular among small and medium-sized enterprises.

In addition, while higher levels of employment have been achieved, employment rates in many euro area countries still fall short of the Lisbon target of 70% and continue to be low compared with other OECD countries. Long-term unemployment and unemployment in certain segments of the labour market, especially among young people, remain far too high in several countries. Policies that allow for wage differentiation and increase flexibility in the labour market, such as the expansion of part-time work and temporary agency work, could help to address these problems. Such policies could also assist in alleviating the "insider-outsider" phenomenon in the European labour market. Tax and benefit systems could be further restructured so as to minimise disincentives to employment and investment.[6]

3 The article entitled "Productivity developments and monetary policy", in the January 2008 issue of the ECB's Monthly Bulletin provides a detailed analysis of productivity developments in the euro area.

4 The Directive on services in the internal market – which aims to bolster the freedom of EU companies to establish themselves in other Member States and the free movement of services – was adopted by the European Parliament and the Council in December 2006, and must be transposed by the Member States into national law by the end of 2009. See "Competition and economic performance of the euro area services sector", in the May 2007 issue of the ECB's Monthly Bulletin.

5 For a detailed analysis of the degree of competition in the euro area services sector and its effects on labour productivity and prices, see the article entitled "Competition and economic performance of the euro area services sector", in the May 2007 issue of the ECB's Monthly Bulletin.

6 For a review of recent structural developments in the euro area labour markets, see the article entitled "Developments in the structural features of the euro area labour markets over the last decade", in the January 2007 issue of the ECB's Monthly Bulletin.

Looking ahead, increasing labour supply and employment would help to counter the economic and budgetary effects of population ageing. In this regard, countries must also take measures to ensure that public finances are sustainable, by speeding up the pace of budgetary consolidation, further reforming pension and health care systems and shifting public spending and revenues towards more productive uses.

Continuing with reform efforts is key

Overall, it is essential to ensure that euro area countries continue to pursue macroeconomic policies aimed at enhancing growth and employment, maintaining sound and sustainable fiscal positions and improving the efficiency of public spending and revenues in order to address the issues reported above. Well-designed structural policies, which promote flexibility in product and labour markets, enhance education and training and foster research and development, are crucial for the long-run performance and smooth functioning of an economy. This is particularly true of a monetary union like the euro area, in which national monetary and exchange rate policies can no longer be used as adjustment mechanisms.[7] The Lisbon strategy for growth and jobs provides the right framework for the euro area countries to accelerate structural reform efforts. It is now crucial that the reform agenda is put into practice.

7 See N. Leiner-Killinger, V. López Pérez, R. Stiegert and G. Vitale, "Structural Reforms in EMU and the Role of Monetary Policy", ECB Occasional Paper No 66, July 2007.