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Recommendation for a

COUNCIL RECOMMENDATION

on Italy's 2012 national reform programme

and delivering a Council opinion on Italy's stability programme for 2012-2015

{SWD(2012) 318 final}

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THE COUNCIL OF THE EUROPEAN UNION,

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

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

Having regard to Regulation (EU) No 1176/2011 of the European Parliament and of the Council of 16 November 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[3],

Having regard to the resolutions of the European Parliament,[4]

Having regard to the conclusions of the European Council,

Having regard to the opinion of the Employment Committee,

After consulting the Economic and Financial Committee,

Whereas:

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

(2) On 13 July 2010, the Council adopted a recommendation on the broad guidelines for the economic policies of the Member States and the Union (2010 to 2014) and, on 21 October 2010, adopted a decision on guidelines for the employment policies of the

1 OJ L 209, 02.08.1997, p. 1
2 OJ L 306, 23.11.2011, p. 25
3 COM(2012)318 final
4 P7_TA(2012)0048 and P7_TA(2012)0047

Member States[5], which together form the 'integrated guidelines'. Member States were invited to take the integrated guidelines into account in their national economic and employment policies.

(3) On 12 July 2011, the Council adopted a recommendation on Italy's national reform programme for 2011 and delivered its opinion on Italy's updated stability programme for 2011-2014.

(4) On 23 November 2011, the Commission adopted the second Annual Growth Survey, marking the start of the second European Semester of ex-ante and integrated policy coordination, which is anchored in the Europe 2020 strategy. On 14 February 2012, the Commission, on the basis of Regulation (EU) No 1176/2011, adopted the Alert Mechanism Report[6], in which it identified Italy as one of the Member States for which an in-depth review would be carried out.

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

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

(7) On 30 April 2012, Italy submitted its stability programme covering the period 2012-2015 and its 2012 national reform programme. In order to take account of their interlinkages, the two programmes have been assessed at the same time. The Commission has also assessed in an in-depth review, under Article 5 of Regulation (EU) No 1176/2011, whether Italy is affected by macroeconomic imbalances. The Commission concluded in its in-depth review[7] that Italy is experiencing imbalances, although not excessive. In particular, while the public debt is already under close scrutiny in the Stability and Growth Pact, macroeconomic developments in the area of export performance deserve attention so as to reduce the risk of adverse effects on the functioning of the economy.

(8) Based on the assessment of the stability programme pursuant to Article 5(1) of Council Regulation (EC) No 1466/97, the Council is of the opinion that the macroeconomic scenario underlying the programme is plausible, under the assumption of no further worsening in financial market conditions. In line with the Commission's spring 2012 forecast, it expects real GDP to contract sharply this year and recover gradually in 2013. In compliance with the Excessive Deficit Procedure (EDP), the objective of the budgetary strategy outlined in the programme is to bring the general government deficit below the 3% of GDP reference value by 2012, based on further expenditure restraint and additional revenues. Following the correction of the

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5 Council Decision 2012/238/EU of 26 April 2012

6 COM(2012) 68 final

7 SWD(2012)156 final

excessive deficit, the programme confirms the medium-term budgetary objective (MTO) of a balanced budgetary position in structural terms, which adequately reflects the requirements of the Stability and Growth Pact. It plans to achieve it in 2013, i.e. one year earlier than targeted in the previous stability programme. Based on the (recalculated) structural deficit[8], the planned average annual fiscal effort over the period 2010-2012 is well above the 0.5% of GDP recommended by the Council under EDP. The envisaged pace of adjustment in structural terms in 2013 allows achieving the MTO in that year and the planned rate of growth of government expenditure, taking into account discretionary revenue measures would comply with the expenditure benchmark of the Stability and Growth Pact. The programme projects the government debt ratio to peak in 2012 and to start declining at an increasing pace thereafter, as the primary surplus increases. In 2013-14 Italy will be in transition period and its budgetary plans would ensure sufficient progress towards compliance with the debt reduction benchmark, as also confirmed in the Commission's 2012 spring forecast. According to plans, the debt reduction benchmark will be met at the end of the transition period (2015). Reaching the above deficit and debt outcomes will require strict and full budgetary implementation of the corrective measures adopted in 2010-11. Finally, Italy appears to be at medium risk with regard to the sustainability of public finances in the long term.

(9) As regards the fiscal framework, the Italian Parliament approved a bill introducing a balanced budget rule in the Italian Constitution. Implementing legislation will be needed to specify key features of the rule, i.e. the modalities of application and the appropriate correction mechanisms and escape clauses as well as the necessary coordination between the different levels of government. The government committed to pursue a durable improvement of the efficiency and quality of public expenditure through in-depth spending reviews at all levels of government. The reviews should also allow prioritising expenditure items in favour of growth. With the same aim, a reorientation of the use of structural funds is underway through measures taken in March 2011 and with the 2011 November's Cohesion Action Plan, which also aims at speeding up the absorption of structural funds. However, important deficiencies in terms of administrative capacity continue to hamper absorption and hence the implementation of the Plan, notably in the convergence regions.

(10) The structure of the tax system and the high level of tax evasion and undeclared work have adversely affected the economic performance of the country. Tax compliance and governance are also affected by wide-ranging tax expenditures and complex and burdensome administrative procedures. The partial shift in tax burden away from the factors of production onto consumption and property already enacted is an important first step to make the tax structure more growth friendly, but a further shift is warranted, while keeping into consideration distributional effects.

(11) The social partners' agreement of June 2011 to reform the wage-bargaining framework has been formalised in legislation. It should allow more extensive use of firm-level contracts, taking better account of the needs of specific production activities.

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[8] Cyclically adjusted balance net of one-off and temporary measures, recalculated by the Commission services on the basis of the information provided in the programme, using the commonly agreed methodology.

However, to fully address the issue of more dynamic nominal unit labour costs than its trade partners, which is a key factor for Italy's competitiveness loss, the wage-bargaining system should be reformed further by allowing more flexible arrangements also at the national sectoral level. In April 2012, the government proposed an ambitious labour market reform addressing long-standing challenges in the Italian labour market, including its segmentation. This reform needs to be adopted as a matter of urgency, ensuring that its objective and level of ambition remains commensurate to the challenge of the Italian labour market. The scale and effectiveness of the liberalisation of employment services should be closely monitored.

(12) Despite efforts made to improve the employability of women, mainly through targeted fiscal incentives, the employment rate of Italian women is significantly lower (46.5% in 2011) than the EU 27 average (58.5% in 2011). Further action on childcare and elderly care facilities is needed. The challenge is particularly big for older female workers in the private sector, as the pensionable age for women will rise by five years between 2012 and 2018.

(13) Youth unemployment in Italy reached 29.1% on average in 2011 and rose further in the first months of 2012. In particular, the unemployment rate among tertiary graduates is high and there is mismatch between the acquired skills and those that are needed in the labour market. The promotion of apprenticeship as a main port of entry into the labour market is welcome but still requires enforcement of the appropriate instruments such as a new system of occupational and training standards and skills certification schemes. The Commission launched an Action Team to reprogramme cohesion funds towards measures that support the employment of young people and the development of SMEs.

(14) The early school leaving rate of 18.8% at national level, with strong regional variations, has adverse effects on youth unemployment. More targeted and coordinated action to address the challenge of early school leaving should be taken by combining prevention, intervention and compensation measures. The underperformance of the tertiary-education system should be addressed including through the full implementation of the 2010 university reform, and a stronger link between universities' performance and the allocation of public funding.

(15) Italy has adopted important measures to liberalise services, in particular professional services, and improve competition in the network industries. However, multiple challenges remain in the energy and transport sectors, in particular railways and ports, where infrastructure and market bottlenecks remain significant.

(16) Although some measures have already been adopted to encourage administrative simplification, the business environment in Italy remains complex. In particular, the judiciary system suffers from a number of inefficiencies in terms of resource utilisation, procedures and institutional organisation that are reflected in the low performance of the Italian civil justice, in particular as regards the excessive duration of case-handling and the amount of backlogs.

(17) Access to financing by SME is difficult and venture capital intensity is weak. An Allowance for new Corporate Equity (ACE) was introduced in December 2011 allowing companies to exclude the notional return on new injections of equity capital from taxable income. This is expected to facilitate the increase in firm size of SMEs

and investment in innovation. While some measures have been taken to foster private R&D, notably the refinancing of the tax credit for business investment in research, the intensity remains low and implementation of projects of an innovative nature is weak.

(18) Italy has made a number of commitments under the Euro Plus Pact. These commitments, and the implementation of the commitments presented last year, relate to fostering employment, improving competitiveness, enhancing sustainability of public finances and reinforcing financial stability. The Commission has assessed the implementation of the Euro Plus Pact commitments. The results of this assessment have been taken into account in the recommendations.

(19) In the context of the European Semester, the Commission has carried out a comprehensive analysis of Italy's economic policy. It has assessed the stability programme and national reform programme, and presented an in-depth review. It has taken into account not only their relevance for sustainable fiscal and socio-economic policy in Italy but also their compliance with EU rules and guidance, given the need to reinforce the overall economic governance of the European Union by providing EU-level input into future national decisions. Its recommendations under the European Semester are reflected in recommendations (1) to (7) below.

(20) In the light of this assessment, the Council has examined Italy's stability programme, and its opinion[9] is reflected in particular in recommendation (1) below.

(21) In the light of the results of the Commission's in-depth review and this assessment, the Council has examined Italy's national reform programme for 2012 and Italy's stability programme. Its recommendations under Article 6 of Regulation (EU) No 1176/2011 are reflected in recommendations (1) to (7) below.

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

1. Implement the budgetary strategy as planned, and ensure that the excessive deficit is corrected in 2012. Ensure the planned structural primary surpluses so as to put the debt-to-GDP ratio on a declining path by 2013. Ensure adequate progress towards the medium-term budgetary objective, while meeting the expenditure benchmark and making sufficient progress towards compliance with the debt reduction benchmark.

2. Ensure that the specification of the key features of the Constitutional balanced budget rule, including appropriate coordination across levels of government, is consistent with the EU framework. Pursue a durable improvement of the efficiency and quality of public expenditure through the planned spending review and the implementation of the 2011 Cohesion Action Plan leading to improving the absorption and management of EU funds, in particular in the South of Italy.

3. Take further action to address youth unemployment, including by improving the labour-market relevance of education and facilitating transition to work, also through incentives for business start-ups and for hiring employees. Enforce nation-wide recognition of skills and qualifications to promote labour mobility. Take measures to reduce tertiary-education dropout rates and fight early school leaving.

[9] Under Article 5(2) of Council Regulation (EC) No 1466/97.

4. Adopt the labour market reform as a priority to tackle the segmentation of the labour market and establish an integrated unemployment benefit scheme. Take further action to incentivise labour market participation of women, in particular through the provision of child and elderly care. To boost cost competitiveness, strengthen the link between wages set at sectoral level and productivity through further improvements to the wage setting framework, in consultation with social partners and in line with national practices.

5. Pursue the fight against tax evasion. Pursue the shadow economy and undeclared work, for instance by stepping up checks and controls. Take measures to reduce the scope of tax exemptions, allowances and VAT reduced rates and simplify the tax code. Take further action to shift the tax burden away from capital and labour to property and consumption as well as environment.

6. Implement the adopted liberalisation and simplification measures in the services sector. Take further measures to improve market access in network industries, as well as infrastructure capacity and interconnections.

7. Simplify further the regulatory framework for businesses and enhance administrative capacity. Improve access to financial instruments, in particular equity, to finance growing businesses and innovation. Implement the planned reorganisation of the civil justice system, and promote the use of alternative dispute settlement mechanisms.

Done at Brussels,

For the Council
The President