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Recommendation for a

COUNCIL RECOMMENDATION

on Germany's 2012 national reform programme

and delivering a Council opinion on Germany's stability programme for 2012-2016

{SWD(2012) 305 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 the recommendation of the European Commission[2],

Having regard to the resolutions of the European Parliament[3],

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 Member States[4], which together form the 'integrated guidelines'. Member States were invited to take the integrated guidelines into account in their national economic and employment policies.

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1 OJ L 209, 02.08.1997, p. 1
2 COM(2012)305 final
3 P7_TA(2012)0048 and P7_TA(2012)0047
4 Council Decision 2012/238/EU of 26 April 2012

(3) On 12 July 2011, the Council adopted a recommendation on Germany's national reform programme for 2011 and delivered its opinion on Germany'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[5], in which it did not identify Germany 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 inclusion in their stability or convergence programmes and their national reform programmes.

(7) On 18 April 2012, Germany submitted its stability programme for the period 2012-2016 and, on 12 April 2012, its 2012 national reform programme. In order to take account of their interlinkages, the two programmes have been assessed at the same time.

(8) According to the first 2012 notification of deficit and debt figures by Germany for the years 2008-2011 for the application of the excessive deficit procedure (EDP), the general government deficit in 2011 was below the 3% of GDP reference value of the Treaty. Moreover, the Commission's 2012 spring forecast projects the general government deficit to stay below the reference value of the Treaty and to further decline over the forecast period. As a result, and in line with the provisions of the Stability and Growth Pact, on 30 May the Commission adopted a recommendation for a Council decision abrogating the decision on the existence of an excessive deficit under Article 126(12) of the Treaty.

(9) Based on the assessment of the stability programme pursuant to Council Regulation (EC) No 1466/97, the Council is of the opinion that the macroeconomic scenario underpinning the budgetary projections in the programme is plausible. The programme's projections for 2012-13 are broadly in line with the Commission's 2012 spring forecast as regards the pace and pattern of economic growth as well as labour market developments. The programme's projections for economic growth in the outer years are broadly in line with the Commission's estimate of Germany's medium-term potential growth rate. The objective of the budgetary strategy outlined in the programme is to meet the medium-term budgetary objective (MTO) already in 2012 and to reach virtually balanced nominal budgets as from 2014, starting from a nominal deficit of 1.0% of GDP in 2011, thus below the 3% of GDP reference value of the Treaty significantly ahead of the 2013 deadline. The programme specifies the previous

[5] COM(2012) 68 final

MTO of a structural deficit of ½% of GDP, (interpreted as a narrow range around 0.5% of GDP), which adequately reflects the requirements of the Stability and Growth Pact, to imply a deficit not exceeding 0.5% of GDP. Risks to the deficit and debt targets may arise notably if additional measures to stabilise the financial sector turned out to be required. Based on the (recalculated) structural deficit[6], Germany plans to respect its MTO throughout the programme period, which should also be the case taking into account the risk assessment. According to the information provided in the programme and also taking into account the risk assessment, the growth rate of government expenditure, taking into account discretionary revenue measures, would exceed the expenditure benchmark of the Stability and Growth Pact in 2012, while respecting it in 2013. Gross debt is planned to increase by 0.8 pp. to 82.0% of GDP in 2012, before falling to 80% of GDP in 2013 and remaining on a downward path thereafter. Following the correction of the excessive deficit, Germany is in a transition period and, according to plans, is making sufficient progress towards compliance with the debt reduction benchmark of the Stability and Growth Pact.

(10) The federal government has taken measures to improve the efficiency of public spending on health care and has proposed a reform of long-term care. Additional efforts to improve efficiency in health care are necessary to contain expected further expenditure increases. The proposed reform of long-term care is also insufficient to cope with expected future cost increases. There is scope for improving the efficiency of the tax system. The federal government is well on track to meet its commitment to increase growth-enhancing spending on education and research. However, it remains important that also the *Länder* and municipalities, which bear the bulk of expenditure on education and research, ensure adequate and efficient spending in these areas. The introduction of the new constitutional debt brake has further strengthened the German fiscal framework. However, there has been no significant progress in the implementation of the budgetary rule at *Länder* level.

(11) Substantial public support for the financial sector, in conjunction with the sector's own adjustment efforts and the beneficial effects of the rebound of the German economy, has stabilised the sector as a whole. Despite the overall relatively stable financial sector and the absence of a credit crunch, there remain weaknesses, in particular, the structural problems of some *Landesbanken*, notably the lack of a viable business model, weak governance structures and vulnerabilities due to a high degree of dependence on wholesale funding.

(12) The good performance of the German labour market, with increasing employment and moderate unemployment, has not benefited all participants to the same extent and wages have not always increased in line with productivity. Fiscal disincentives arising from the high tax wedge, in particular due to the high social security contributions, continue to hinder the integration of low-wage earners in particular into the labour market. Extensive use of mini-jobs leads to low acquisition of pension rights. Therefore, there is a need to improve the transition from mini-jobs to more stable forms of contracts. The recent reform of labour market instruments should support employment opportunities for all. Raising the effectiveness of the education system and the educational achievement of disadvantaged groups is a major challenge for

[6] 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.

Germany. In the medium- to long-term, ensuring the availability of qualified labour will be crucial to mitigate the negative effects of demographic changes on potential growth. The low full-time participation of women in the labour force is a concern. Fiscal disincentives for second earners and the lack of full-time childcare facilities and all-day schools hinder female labour market participation.

(13) Germany is pursuing a major reform of the energy system. The overall economic costs of transforming the energy system should be minimised by accelerating the national and cross-border network expansion, continuously increasing the cost-effectiveness of climate and renewables policies, taking decisive steps to further foster energy efficiency, and raising competition in the energy markets. Given Germany's central geographical position, the German railway system has a significant impact on the overall European railway system. Competition in the passenger and freight rail markets remains very low, mainly due to the lack of effective separation between the infrastructure manager and the railway holding. Despite progress made in recent years, *inter alia* through the implementation of the Services Directive, there is scope to further stimulate competition and productivity growth in some services sectors (e.g. construction).

(14) Germany has made a number of commitments under the Euro Plus Pact. The commitments, and the implementation of the commitments presented in 2011, 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.

(15) In the context of the European Semester, the Commission has carried out a comprehensive analysis of Germany's economic policy. It has assessed the stability programme and national reform programme. It has taken into account not only their relevance for sustainable fiscal and socio-economic policy in Germany 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 (4) below.

(16) In the light of this assessment, the Council has examined Germany's 2012 stability programme, and its opinion[7] is reflected in particular in recommendation (1) below,

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

1. Continue with sound fiscal policies to achieve the medium-term budgetary objective by 2012. To this end, implement the budgetary strategy as envisaged, ensuring compliance with the expenditure benchmark as well as sufficient progress towards compliance with the debt reduction benchmark. Continue the growth-friendly consolidation course through additional efforts to enhance the efficiency of public spending on health care and long-term care, and by using untapped potential to improve the efficiency of the tax system; use available scope for increased and more efficient growth-enhancing spending on education and research at all levels of government. Complete the implementation of the debt brake in a consistent manner

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

across all *Länder*, ensuring timely and relevant monitoring procedures and correction mechanisms.

2. Address the remaining structural weaknesses in the financial sector, *inter alia* by further restructuring of those *Landesbanken* which are in need of an adequately funded viable business model while avoiding excessive deleveraging.

3. Reduce the high tax wedge in a budgetary neutral way, in particular for low-wage earners, and maintain appropriate activation and integration measures, notably for the long-term unemployed. Create the conditions for wages to grow in line with productivity. Take measures to raise the educational achievement of disadvantaged groups, notably through ensuring equal opportunities in the education and training system. Phase out the fiscal disincentives for second earners, and increase the availability of fulltime child-care facilities and all-day schools.

4. Continue efforts to keep the overall economic costs of transforming the energy system to a minimum, including by accelerating the expansion of the national and cross-border electricity and gas networks. Ensure that the institutional set-up guarantees effective competition in railway markets. Take measures to further stimulate competition in the services sectors, including professional services and certain crafts, in particular in the construction sector.

Done at Brussels,

For the Council
The President