Economy Report

Economic Policy

Sustainable Governance Indicators 2020

SGI Sustainable Governance Indicators

BertelsmannStiftung

Indicator

Economic Policy

Question

How successful has economic policy been in providing a reliable economic framework and in fostering international competitiveness?

41 OECD and EU countries are sorted according to their performance on a scale from 10 (best) to 1 (lowest). This scale is tied to four qualitative evaluation levels.

10-9 = Economic policy fully succeeds in providing a coherent set-up of different institutional spheres and regimes, thus stabilizing the economic environment. It largely contributes to the objectives of fostering a country's competitive capabilities and attractiveness as an economic location.

8-6 = Economic policy largely provides a reliable economic environment and supports the objectives of fostering a country's competitive capabilities and attractiveness as an economic location.

5-3 = Economic policy somewhat contributes to providing a reliable economic environment and helps to a certain degree in fostering a country's competitive capabilities and attractiveness as an economic location.

2-1 = Economic policy mainly acts in discretionary ways essentially destabilizing the economic environment. There is little coordination in the set-up of economic policy institutions. Economic policy generally fails in fostering a country's competitive capabilities and attractiveness as an economic location.

Denmark

Score 9

Output is currently slightly above capacity output (positive output gap). Employment has been growing, especially for the elderly, and unemployment is close to the structural level, which is comparatively low. Per capita income has increased more than in most other countries, not least due to improvements in the terms of trade. Productivity growth is low by historic comparison, but similar to the OECD average. Growth in GDP is projected to slow down a little over the coming years from about 2%. The growth forecast for 2020 is about 1.25%, comparable to growth in many other OECD countries.

The public budget is in surplus, reflecting the favorable business cycle situation, and the structural balance is close to zero. Public debt is (EMU debt) is about 35% of GDP, which is low in comparison to most EU member states. Fiscal policies are sustainable despite an aging population due to mandated labor market pensions and recent reforms to increase statutory retirement ages.

The Danish labor market is characterized by rather high levels of turnover and flexibility. Remaining unemployment is mainly structural and concentrated on specific groups, mainly low-skilled workers (among whom immigrants are overrepresented). The social safety net and labor market policies have recently been reformed to strengthen work incentives. Structural discussions have focused on ensuring that the labor force comprises an appropriate mix of qualifications and improving the position of immigrants in the labor market. Efforts to improve productivity raise questions concerning education, research, industrial and tax policies.

While the conditions for fiscal sustainability are being met, political discussions about the appropriate balance between tax revenue and expenditure continue. On the expenditure side, there is widespread discussion about demographic change (e.g., population aging) and increasing demand for social services, not least on healthcare. The new Social Democratic government, which came to power at the end of June 2019, is planning to increase spending on welfare and education in 2020. A major policy question concerns the setting of ambitious environmental goals, the financing of the measures needed to reach these goals and the broad consequences of these measures for the economy.

Geopolitical developments, including the United Kingdom’s Brexit decision, are a source of uncertainty for the future development of the Danish economy.

Citation:
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Luxembourg

Score 9

GDP in Luxembourg was expected to increase by 3% in real terms in 2019. This means the country is growing significantly faster than the euro zone average.

Growth engines include goods and services exports, which were expected to grow by 3.2% in 2018 and 2.7% in 2019. Investment (+3.2%) and private consumption (+3.5%) were even more important in 2019. In real terms, imports were forecast to increase by 2.6% in 2019. Overall domestic demand increased by 2.4% in real terms in 2018 and was expected to increase by 2.1% in 2019, according to the European Commission.

Luxembourg’s real GDP collapsed by 5.6% during the crisis years of 2008 and 2009. However, the economy has grown continuously since. By 2017, price-adjusted GDP was 18.2% higher than before the recession in 2007. By comparison, this level has increased by only 8.6% across the EU as a whole.

Luxembourg’s population increased by 24.4% between 2008 and 2018. The Eurostat statistics office expects a further increase of 21.3 by 2028%. The strong influx of mostly well-educated workers is increasing the long-term demand for goods and services of all kinds.

According to the EU Commission, investment in Luxembourg was expected to increase by 3.2% in 2019 in real terms.

Luxembourgish private consumption was forecast to increase by 3.5% in 2019, according to the European Commission. This robust demand has helped drive strong increases in the number of those employed, by 3.6% in 2018 and a predicted 3.3% in 2019. Real wages have risen moderately over the same period, by 0.6% (2018) and 0.5% (2019). However, as a result of the influx of workers, real-estate prices are rising sharply, reducing the disposable income available for private consumption. Nevertheless, Luxembourg's per capita consumer expenditure in 2017 of €28,400 was by far the highest such level in the EU.

Luxembourg's trade deficit increased by 16.6% in 2017. Since the country's industrial sector has lost much of its importance in recent decades, dependence on imported goods is high. In 2017, 31.9% of imports came from Belgium, with Germany (24.9%) and France (11.4%) also serving as key countries of origin. The most important foreign market in 2017 was Germany, with an export share of 25.5%, ahead of Belgium (17.4%) and France (14.2%).

Various industries outside the financial sector also make significant contributions to the country's economic stability and innovation. With its political and economic cluster initiative, the Grand Duchy is promoting seven non-financial industrial sectors. These include audiovisual production, the digital economy, health and environmental technologies, the aerospace industry, shipping, and the automotive supply industry.

In addition, Luxembourg's government is pursuing various strategies to increase the country's attractiveness as a business location. Key activities include the provision of support for the fintech sector, the passage of cybersecurity measures, the digitalization of the public administration and the development of the country's technological infrastructure. With more than 20 data centers in place today, Luxembourg is already one of the largest data and internet hubs in Europe.

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Malta

Score 9

Economic planning is at the forefront of Malta's policymaking process and a clear-cut assignment of tasks to government institutions is its strength. Strong ties between public institutions, the economic planning ministry, and social partners exist through the Malta Council for Economic and Social Development (MCESD). This system has provided the ideal foundation for strong economic performance. Indeed, provisional GDP estimates for the second quarter of 2019 indicate an increase of 6.6% over the same period in 2018, and a 4.4% increase in volume terms. Moving forward, momentum is set to remain solid but moderate throughout 2019 and 2020. The European Commission's 2019 autumn economic forecast continues to place Malta's economic growth among the highest in the EU, with GDP growth expected to be 4.2 % in 2020 and 3.8 % in 2021. Malta's received a score of 68.6 on the Heritage Foundation's 2019 Index of Economic Freedom, giving it an overall rank of 41st place. In Europe, Malta is ranked 20th out of 44 countries, a score which corresponds to the regional average.

The shift toward the provision of internationally focused services has undoubtedly contributed to the country's economic prosperity. Malta's labor market remains resilient, and the country's unemployment rate is currently among the European Union's lowest. Indeed, increased employment rates have led to higher levels of disposable income. Public consumption and investment in the first half of 2019 were also substantial. As a result, domestic demand replaced net exports as the principal driver of economic growth. Industrial legislation provides protection against dismissals and allows for open bargaining between employers and their unions, but with few codetermination structures. Unit labor costs have increased moderately, but are projected to accelerate at a faster rate in the coming period.

Moody's credit-rating agency upgraded Malta's rating from A3 to A2 for the first time in 11 years in view of the positive economic performance. However, the country's ranking fell from 36th to 38th. Nonetheless, the country was ranked first globally in terms of macroeconomic stability, and 25th in the context of ICT adoption.

The country continues to work to improve its ease of doing business. In a bid to ensure a more efficient and responsive business climate, and to reduce the administrative burden for investors setting up businesses in Malta, the government has created the position of commissioner for simplification and reduction of bureaucracy. Furthermore, it has established five one-stop-shops to assist businesses in the acquisition of information and services. This has been coupled with the creation of the Start-Up Malta Foundation (SUM) to assist nascent and established startups. The government is also working to diversify the economy and attract investment in leading technologies. For example, Malta's parliament has officially approved the Production of Cannabis for Medicinal Use Act in order to provide the necessary regulations for the production and prescription of this substance, and is seeking to transform the island into a center of excellence for blockchain technology, which experts believe will be a leading growth engine in the future. Significantly, in July 2018, Malta became the first country in the world to implement a regulatory framework for stakeholders in the blockchain, cryptocurrency and distributed ledger technology sectors. Nonetheless, no licenses have been issued to date. Malta ranked 10th in the EU Commission digital economy index.

Rapid economic growth has brought several challenges to the fore. First is the continued dependence on financial services and property development. Second, this growth has sparked a massive building program and consequent import of labor, while also increasing demands on infrastructure and social services to a degree that may prove unsustainable for an island country measuring just 316 square kilometers. An IMF review mission cautioned against the risks associated with the country's fast-paced growth. This is coupled with increasing concerns among the general public regarding the prospect of overdevelopment. Finally, Malta ranked only 20th among EU member states on the U.N. Sustainability Index, registering no improvement on key indicators such as the quality of overall infrastructure and sea cleanliness.

Citation:
National Statistics Office (NSO) News Release 145/2019
European Economic Forecast Summer 2019 (Interim) p.20
TVM 30/08/2019 Malta with Fourth-Lowest Unemployment Rate Among EU Countries
Commission Staff Working Document – Country Report Malta 2019 SWD (2019) 1017 final p. 7
Times of Malta 20/07/2019 Moody's Upgrades Malta's rating for First Time in 11 Years
World Economic Forum Global Competitiveness Report 2019
Doing Business 2019 – Training for Reform p.5
https://simplification.gov.mt/en/Pages/home.aspx
Pre-Budget Document 2020 p. 49
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Forbes 05/07/2018 Maltese Parliament Passes Laws That Set Regulatory Framework for Blockchain, Cryptocurrency And DLT
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The Malta Chamber of Commerce 09/09/2019 Trade Deficit Widens by €675M in First Seven Months of 2019
Malta Today 16/01/2019 Malta's Strong Economy Faces Infrastructure, Housing and Labour Challenges – IMF
Times of Malta 07/09/2019 Protesters March Against the Beat of Developers' Drum in Valletta
Times of Malta 02/07/2019 Malta Ranks 20th in EU on Sustainable Development Goals
Business Malta 13/06/19 Malta ranks 10th on EU Digital and Sociey Index
https://ec.europa.eu/info/business-economy-euro/economic-performance-and-forecasts/economic-performance-country/malta/economic-forecast-malta_en
2019 index of economic freedom https://www.heritage.org/index/country/malta

Netherlands

Score 9

The Dutch economy grew by 2.8% in 2018, the sixth consecutive year of considerable positive economic growth. Overall, conventional indicators of the economic cycle are performing well – indeed, they are the highest among EU member states, according to the World Economic Forum's Global Competitiveness Report (GCR) 2019. Trust indicators for business and consumers have declined from a peak in early 2018, but (in December 2018) are still quite optimistic.

The economy's international standing has been steady, with the Netherlands ranking fourth out of 141 countries in the 2019 GCR, only behind Hong Kong, the United States and Singapore. The Netherlands scores highly in the areas of macroeconomic stability, health, infrastructure quality and business dynamism. However, its performance has slightly declined with respect to infrastructure, labor-force skill levels, product-market efficiency (especially the complexity of tariffs) and innovation capability.

In sum, although the Netherlands was caught in a long-term slump, strong economic recovery since 2013 has now led to a booming economy. Nevertheless, in terms of the euro zone, Dutch economic performance is average. Political debate on economic policy has turned strongly toward issues of inequality, and especially the well-documented fact that in spite of the country's satisfactory macroeconomic performance and well-balanced state budget, Dutch households have yet to experience serious improvements in recent years with regard to consumption spending and quality of life.

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Sweden

Score 9

Over the past several years, the Swedish economy has been exceptionally strong. Growth in terms of GDP in 2017 and 2018 was 2.3%. For 2019, GDP growth is expected to be somewhat weaker, mainly due to the impending international recession. In 2020 and 2021, the GDP growth rate is expected to be approximately 1.5%. As a highly trade-dependent economy, Sweden's economic development is sensitive to fluctuations in international markets.

Notwithstanding, most long-term economic indicators on Sweden assuage concern; particularly with regard to international competitiveness. Thus, it is fair to say that the institutional and regulatory framework of the Swedish economy provides basic stability and predictability. However, there are some challenges. The National Bank of Sweden, fearing deflationist tendencies in the economy, lowered its "steering interest rate" to an unprecedented 0% in late October 2014, then to -0.35% in September 2015. By November 2016, the interest rate had fallen to -0.5%, which is also the interest rate level in October 2019. In addition, the inflation rate remains below the National Bank of Sweden's target.

Another concern is household debt, which remains high. There are also growing fears (e.g., mentioned in an IMF report) of an emerging bubble in the real-estate market. In an attempt to cool the market, the government introduced mandatory mortgage repayment rules and there is discussion on phasing out tax deductions for interest rate payments. Together with increasing construction, these measures would help cool off the real-estate market in metropolitan areas in the longer term. Nonetheless, the current housing shortage in metropolitan areas that is driving real-estate prices up increases the short-term risk of a bubble in the real-estate market. In November 2017, the government announced plans to introduce a mortgage requirement, the exact date is yet to be decided, to help cool the real-estate market and curb household debt.

Economic growth and international competitiveness are closely linked to unemployment and labor-market dynamics. The red-green government committed itself in 2014 to halving the country's unemployment rate (which, at the time, was one of Europe's lowest) by 2020, a target which will be difficult to reach. Unemployment gradually decreased since 2015. In 2018, unemployment fell to approximately 6%. In other European countries, the decline of open unemployment is stronger.

There are now signs on both sides of the political aisle that policymakers might relax their commitment to the regulatory framework that has to date shaped public budgets and the economy. The previous center-right government (2006 – 2014) downplayed the importance of a surplus goal, a stance which the incoming Social Democratic and Green government after the 2014 election has shared. The argument for doing so is that there are urgent programs that require public funding. In 2016, the Social Democratic and Green government negotiated with opposition parties to introduce a reform of the financial framework. The revised framework retains the surplus goal, but at a lowered 0.33% over a business cycle. More importantly, the revised framework states that public debt is to be brought down incrementally.

Moreover, some sectors of the economy, for example the housing market, suffer from low efficiency and lack of transparency. In addition, tax reforms implemented before the last period under review have further undermined economic equality. Nonetheless, Sweden's economy and its regulation thereof are generally considered to be efficient and sound. Whether this is a product of policy incentives, or a consequence of being outside the euro area is a matter debated among economic experts.

Although the institutional and regulatory framework of economic policy remains overall robust and efficient, the governance of that system has proven exceedingly complex since the 2018 general elections. With 62 seats, the Sweden Democrats (SD) party holds a pivotal position between the Social Democratic-Green-Left bloc and the center-right "Alliance." In January 2019, the Social Democratic-Green government negotiated a 73-item agreement ("the January Accord") with the Center

Party and the Liberals in order secure parliamentary passage for major government bills. The agreement indicates a shift toward neoliberal economic policy, including an overhaul of the tax system and re-evaluation of public services across a large number of policy areas.

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Canada

Score 8

In its fall 2019 Monetary Policy Report, the Bank of Canada projected real GDP growth of 1.7% in 2020, a slight increase from 1.5% in 2019. Real gross domestic income (GDI) growth, which takes changes in terms of trade into account, slowed in 2019 to a growth of 1.6%, down from last year’s 2%. Projections for 2020 are slightly lower, at 1.5%. This slowdown of growth can be attributed to a reduction in business investment and exports due to global uncertainty, combined with a decline of investment in the energy sector stemming from transportation constraints. These constraints are expected to ease as pipeline and rail capacity gradually expand.

Canada has implemented market-oriented policies that have enhanced the country’s attractiveness to business. Yet there are areas where Canada’s economic framework could be more conducive to productivity growth, as described in the 2020 World Bank Doing Business Report, which ranked Canada 23rd out of 190 countries for the overall ease of doing business, down from eighth place out of 181 countries in 2009.

A key challenge for Canada involves the coordination of regulatory policy across federal and provincial jurisdictions, exacerbated by the presence of interprovincial barriers to trade and labor mobility. In many areas, effecting change requires cooperation between different levels of government, which frequently impedes progress.

Another factor is the country’s dependence on natural resources, which account for roughly 20% of GDP. Aside from the risks associated with the high levels of price volatility in this sector, uncertainties regarding policies and regulations surrounding major projects (e.g., the duty to consult with Indigenous groups) have the potential to stall investment. This factor may be mitigated by the current Liberal government's new Bill C-69 (the Environmental Assessment Act), which is aimed at reducing uncertainty in large-scale projects. The effectiveness of the bill has yet to be demonstrated, however.

Another issue affecting Canada's competitiveness is the role played by marketing boards, which set production quotas. While these issues came to the fore during the recent NAFTA renegotiations, no major party has made a commitment to significantly reduce these barriers.

Household debt levels remain high. The current ratio of household debt to disposable income in Canada is above 177%, and housing affordability continues to decline. Although the federal government has repeatedly tightened mortgage-lending rules in recent years, and provincial governments have enacted legislation to curb real-estate investment by foreign entities, housing markets in Canada's largest cities of Vancouver and Toronto remain unbalanced. A possible correction in the housing market would pose a significant risk. There appears to be room for additional measures to mitigate speculative investment activity, and to improve coordination between federal and provincial regulators.

A final concern focuses on the need for talent and innovative ability. In the World Economic Forum's most recent Global Competitiveness Report, Canada continues to receive low rankings with regard to the quality of education, technological readiness, business sophistication and the capacity to innovate. The federal budgets in 2018 and 2019 attempted to stimulate innovation through the development of "innovation superclusters," but these clusters have not yet made a major impact.

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Finland

Score 8

Having contracted for several years, the Finnish economy is currently experiencing a positive turnaround. The recent economic growth is mainly due to a strong increase in exports. However, the impact of the recession on public finances has been so strong that a full recovery will not be achieved for some time. Unemployment rates continue to be high in comparison with other Nordic countries. Fiscal policy has been a particular concern, as public debt has grown fairly consistently over the last decade as a share of GDP. However, slight decreases have were reported in 2017 and 2018. Government spending accounts for over half of GDP, which is among the highest such ratios in the European Union.

The Sipilä government (2015 – 2019) made efforts to restore economic growth, increase competitiveness and reduce public debt. With the aim of restoring fiscal sustainability, the government placed a priority on greater budgetary prudence and balancing the budget as well as sought to raise the minimum statutory retirement age, while improving incentives for people to continue working into later life. While the Finnish economy has continued to perform fairly well with regard to several measures of economic freedom, the country’s overall performance had been in decline for some years. However, in the Heritage Foundation’s 2019 Index of Economic Freedom, Finland’s economy was ranked 20th, a clear improvement from its 26th-place ranking in 2018. This improvement is attributed to stronger performances in the fields of fiscal health and government spending. Overall, the positive figures concerning the annual GDP growth rate and several other economic indicators are reason for optimism. According to the Economic Survey of the Ministry of Finance in June 2019, the economy was projected to grow by 1.6 % in 2019.

Citation:
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Ireland

Score 8

Despite the overstating of Ireland’s economic performance through the activities of the multinational corporations, the underlying domestic economy performed extremely well in 2019. Proxy indicators such as labor market data, tax revenue, modified investment expenditure and consumption expenditure were all positive. Total employment increased to 2.3 million and unemployment fell to 5.1% of the labor force.

However, against this background of strong economic growth, Ireland faces some serious supply-side constraints, most notably in the area of housing.

In November 2018, the Irish Fiscal Advisory Council (IFAC), which was formally established as a statutory body in December 2012 under the Fiscal Responsibility Act, published its fifteenth Fiscal Assessment Report. The report, under the chairmanship of academic Seamus Coffey, was highly critical of government budgetary policy. It asserted that there had been no improvement in the budget balance, excluding interest costs, since 2015 and maintained that non-interest spending by the government has expanded at the same pace as government revenues. Arguing that a great deal of the improvement in government revenues has been cyclical or temporary, the IFAC report suggested that the overall structural position has deteriorated. Resulting from this, the IFAC report contended that opportunities to strengthen the budget balance during the upswing in the economic cycle have been missed. It identified unbudgeted increases most notably in the area of healthcare as a major problem area and argued that the Health Service Executive (HSE) has exceeded its allocation by almost €2 billion over the previous four years.

In its initial comments on the 2020 budget, IFAC stressed that the economy faces unusual uncertainty on two fronts, namely (1) overheating, because the economy is close to its potential, and (2) Brexit-related issues. IFAC stressed that health over-runs continue despite large planned increases. In the health budget for 2019 an increase of €1.7 billion was planned pushing total health expenditure up to €17 billion. Budget 2020 indicates that, notwithstanding this increase, there was a further over-run of €0.4 billion in 2019 – this unplanned increase repeats the pattern of over-runs in recent years.

Citation:
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Israel

Score 8

As in previous years, while Israel's economic policy has some shortcomings, it is fundamentally strong. It largely provides for a reliable economic environment, renders the country internationally competitive and ensures it remains attractive as a location for economic activity.

According to the Bank of Israel's monetary policy report for the first half of 2019, Israel's economic growth rate is expected to be relatively low at 3%, following a period of deceleration during the second and third quarters of 2018. The report also highlights the large degree of uncertainty regarding fiscal policy, as the coalitional negotiations remain ongoing And yet, the Bank of Israel is positive about Israel's economic performance, and predicts that Israel's economic growth will be 3.1% in 2019 and 3.5% in 2020. Though the inflation rate is projected to be slightly higher than what had been assumed in previous reports (1.6% in 2019 and 2020). For the past year (September 2018 to September 2019), the Bank of Israel calculated the inflation rate to be 0.3%.

The cost of living remains high relative to the OECD average, particularly for housing. Housing prices have increased in recent years, making home ownership hard to attain for young and middle-class people. Yet, the rate of growth declined in

2017, which might have been as a result of aggressive government housing subsidies for middle-class buyers. In addition, rent costs also increased, though not as sharply as ownership costs. This trend mostly affects the middle and lower classes, and was one of the main causes of the 2011 social-justice protest. According to a 2018 OECD report, public transport deficiencies also play a role in worsening the cost of living, as residents of Israel's peripheral areas cannot easily commute to central regions for work despite Israel being a relatively small country.

Regarding international competitiveness, Israel appears to be relatively attractive to foreign investors. According to the latest annual report of Israel's Central Bureau of Statistics, Israel's balance of payments has been positive for over a decade (though with a small decrease since 2015), while the number of foreign investments in Israel has been rising every year. The report also shows that unemployed workers as a percentage of the labor force decreased over the past five years to 4% in 2018. Though the labor force participation rate also decreased over the same period, to 63.9% in 2018.

Citation:
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Latvia

Score 8

After a difficult post-crisis period of economic adjustment in 2009 and 2010, Latvia's economy has fully rebounded and become more resilient, returning to the international markets and to favorable economic growth rates. In the last decade, there have been no significant economic imbalances, only moderate levels of inflation, with economic growth averaging around 3.5% (4.8% in 2018). The OECD has noted that Latvia's economic growth is projected to remain strong, as exports strengthen and EU structural fund transfers boost investment.

Latvia's economic policy had been governed by parameters accepted as part of financial assistance provided by the IMF and the European Union. Even though this assistance has since been repaid and parameters are withdrawn, they have provided a framework in which the economy established fiscal discipline. For example, in 2013, Latvia introduced legislation that placed a cap on the public budget deficit and launched a multi-year planning cycle. The Fiscal Discipline Council (FDC) plays an oversight function, consulting with the government on fiscal planning issues and compliance with the budget deficit cap.

In 2019, while commending the low budget deficit (in comparison with the EU average) as well as the government's setting up a fiscal reserve for 2020 – 2022, the FDC also called for an increase of the reserve in the future urged the government to be more proactive in their counter-cyclical activities.

Since meeting the policy goals of joining the euro zone in 2014, Latvia's focus has shifted to longer-term issues of maintaining competitiveness within the euro zone and addressing social inequalities. Over the coming years, Latvia will need to maintain progress with economic reforms and participate more actively in international trade to ensure continued economic progress. Domestically, there should be a stronger focus on innovation and research and access to jobs.

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Lithuania

Score 8

Lithuania's economic policies have created a reliable economic environment, fostering the country's competitive capabilities and improving its attractiveness as an economic location. In its 2020 Doing Business report, the World Bank ranked Lithuania at 11th place out of 190 countries. The country's position in this rating exceeded the target of 15th place set by the Skvernelis government after the parliamentary elections in late 2016. The criteria assessed most positively included registering property (ranked 4th), enforcing contracts (ranked 7th) and dealing with construction permits (ranked 10th). Meanwhile, resolving insolvency (ranked 89th) was assessed least positively, but the country is working on new insolvency legislation and flanking measures that should make the insolvency framework more effective in the next few years. Lithuania climbed three positions in the 2020 report, from 14th place out of 190 countries in 2019. This is attributable to the fact that obtaining electricity services was made simpler through the launch of an integrated digital application and a reduction in the cost of new connections, as well as to the fact that minority investor protections have been strengthened thanks to the clarification of ownership and oversight structures. In the Global Competitiveness Report 2019, the World Economic Forum ranked Lithuania at 39th place out of 141 countries, with the nation scoring particularly well with regard to its macroeconomic environment (ranked 1st) and ICT adoption (ranked 12th). Here, Lithuania gained one position in the 2019 report. These regulatory improvements have mostly resulted from the focused work of the Ministry of Economy and Innovation. After the formal expansion of the ruling coalition to include two additional parliamentary factions in mid-2019, several new tax-introduction initiatives were added to the government agenda. This created significant uncertainty during the debates over the draft state budget for 2020, and led to complaints by the main business associations that the government had broken its agreement with social partners regarding the stability of the tax regime.

The European Commission has identified the following challenges to Lithuania's long-term competitiveness: unfavorable demographic developments, labor market deficiencies and high emigration rates, growing levels of poverty and social exclusion, a lack of competition and interconnections in the country's infrastructure (particularly its energy system), low energy efficiency (especially in the case of buildings), a low level of R&D spending, and poor performance with respect to innovation. Recent increases in energy prices and increasing wages in the labor market have made it more difficult for Lithuanian companies to maintain their competitiveness, in particular under the relatively restrictive labor-immigration regime. Further infrastructural integration projects – including the construction of links between the Baltic states' electricity systems and those of Central Europe through Poland, withdrawal from BRELL (the Russian-managed electricity grid) by 2025, and the construction of a natural-gas connection to Poland by 2021 – are high on the agenda of the current government.

The Skvernelis government was also able to push through a few important reforms, including changes to the tax system and the second pillar of the pension system. Although reducing the overall tax burden on labor will have a negative short-term effect on state and municipal revenues, the implementation of these structural reforms was expected to increase the annual GDP growth rate by an average of 0.3% between 2019 and 2030 (assuming the reforms are in fact implemented). However, as noted above, some of these reform decisions, including the reduction of the tax burden on labor, have already been revised or delayed; this stems from proposals by newly elected President Gitanas Nausėda to fund his proposal for old-age pension increases by increasing taxes, as well as proposals by some coalition partners to impose additional taxes on financial institutions such as banks in order to increase child benefits and other budgetary expenditures. Many analysts and business representatives criticized the process of debating tax-code changes during the 2020 budget process as chaotic.

Streamlining the regulatory environment for businesses is one of the few areas where some progress has been achieved, especially in terms of the number of procedures and days required to start a new business. However, inefficient government bureaucracy remains the second-most-problematic factor with regard to doing business in the country, according to surveyed business executives. In the Global Competitiveness Report 2019, the World Economic Forum ranked Lithuania at 85th place out of 141 countries with regard to the burdens imposed by government regulation, and 91st with regard to the efficiency of the legal framework in challenging regulations. Additional efforts are necessary to promote Lithuania's transition to a circular economy, as the country's economy remains very resource-inefficient, with landfill remaining the cheapest way of treating industrial waste.

Citation:
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Switzerland

Score 8

The Swiss economy is highly competitive, ranking again at the top – five out of 141 countries – in the World Economic Forum's 2019 competitiveness assessment. Switzerland has the third-highest GDP per capita in the OECD, which the OECD links to the country's high employment rates and productivity levels. According to the OECD, these factors support, and are supported by, good health outcomes and an education system that delivers graduates with high performance scores.
The country's economic policy regime combines a variety of mechanisms. Common denominators, however, are the practice of muddling through as standard operating procedure and heterodoxy as the primary philosophy underlying economic policymaking.

For example, regulation of the labor market is very liberal, particularly with regard to hiring and firing. In contrast, government policies were quite illiberal and politicized with regard to the flow of foreign labor and with regard to farming in the past. The policymaking process previously emphasized the integration of employers and trade unions, with employers enjoying considerable influence ("liberal corporatism") and trade unions serving as junior partners. For trade unions, this corporatism made sense since it resulted in full employment (at least for Swiss citizens), high wages and generous employer-sponsored benefits. While this influence was strong in the past, in recent years the influence of both organized labor and capital has lessened, but it is still a major aspect of Swiss economic policymaking.

Throughout the 20th century, Switzerland maintained a very protectionist policy regime, allowing for cartels and monopolies. The main beneficiaries were farmers, who were protected from global competition by high tariffs and strict non-tariff barriers, as well as small- and medium-sized businesses and service providers producing for the domestic market. Collusive pricing was tolerated, while competition between providers and producers was limited by the diversity of cantonal regulations.

This policy of protectionism has lessened considerably since the mid-1990s due to a deliberate strategy of market liberalization. At the same time, there has been continuous pushback to this liberalization. For example, an amendment to the law on cartels failed. It would have reduced the influence of major economic actors within the competition agency's governing board. Similarly, farmers were successful in being spared from austerity measures; they continue to enjoy a comparatively high level of protection.

Between 1960 and 2005, Swiss real GDP growth rates have exceeded the average of the 23 advanced-democratic OECD nations in only nine of 44 years. Between 2005 and 2014, Swiss economic growth rates were above average; since 2015 they have returned average or below average. Some economists have attributed the Swiss economy's strong growth since about 2005 to its liberalizing reforms. Others note that most of the increase in domestic product is not due to higher productivity, but rather to the increasing volume of hours worked, which itself is at least partially a result of population growth (1% per year, mostly due to immigration). With very few exceptions, Switzerland's current account balance has been positive since the 1970s, implying that exports exceed imports. In the second quarter of 2019, the balance was 12% of GDP, while Germany, for example, recorded 7% of GDP. Switzerland's main export industries are the chemical, pharmaceutical and metal industries (e.g., machines and watches). A considerable share of recent economic growth is therefore export-driven, making Switzerland very dependent on export markets. The country's persistently rocky relationship with the European Union poses imminent dangers to the continued success of its export-oriented economy. However, Swiss economic growth is very robust. Although the Swiss franc appreciated considerably following the decision of the Swiss National Bank to abandon the peg to the euro in January 2015, the impact on the national economy has been limited.

The government levies low taxes on both labor and capital, producing relatively small tax wedges. In addition, the state does not significantly intervene in the business cycle. Rather, it traditionally pursued a prudent and largely procyclical fiscal policy. In times of major economic challenges, such as in 2008 and 2009, fiscal stimulation packages have been implemented. However, for institutional and political reasons these packages have typically been very limited in size and proved difficult to implement swiftly. In fact, many of the resources contained in these fiscal programs have not been taken up by employers. Responsibility for price stability is left to the independent National Bank, which is tasked with maintaining price stability as a primary goal, and has the tools of monetary and interest-rate policy at its disposal.

Rather than actively influencing the structure of industry, the government has restricted itself to facilitating the modernization of industries by creating favorable conditions for economic activity. In the financial industry, Switzerland has improved its surveillance of banks and set prudential banking regulations since the onset of the Great Recession in 2008.

In general, decision-makers have pursued a very pragmatic and heterodox economic policy and shown themselves willing to disregard liberal norms of policymaking if the need arises. This policy regime, which has been both liberal and protectionist, has come under pressure due to globalization and the increasing importance of international organizations such as the WTO. Given its reliance on the export of goods and services, Switzerland has had to acquiesce to liberalization.

Liberalization was accelerated by bilateral treaties with the EU and practically all new economic policies have followed EU standards. As a consequence of globalization and Europeanization, most sectors increasingly liberalized, in particular in the period between the mid-1990s and 2005. Agriculture offers a major case in point, though Switzerland's agriculture sector remains one of the most subsidized in Europe.

As a result of liberalization, one of the drivers of Switzerland's postwar economic success – the complementarity of protected domestic-oriented industries and liberal export-oriented industries – has been weakened. The increase in tensions between the export- and domestic-oriented sectors have generally not resulted in open conflict. These developments have, however, increasingly undermined the country's system of interest representation and the corporatist structure of interest intermediation. Interest organizations, in particular employers' groups, have lost support and their members have increasingly turned to lobbying at the level of the individual firm.

Switzerland has not yet determined its long-term relationship with the EU. In the current review period, the quest for politically and economically sustainable solutions became more pressing. Previous interventions entailed bilateral agreements with the EU, which further liberalized the service and agriculture sectors. In addition, immigration policy has changed substantially. Switzerland has abstained from any further recruitment of foreign labor from outside the EU, while liberalizing its immigration regime with EU countries. This policy has meant free movement of labor between Switzerland and the EU, intensifying opposition to the recruitment of highly skilled employees from abroad.

This bilateral arrangement with the EU faces major challenges. The EU has requested new institutional structures to complement and support the bilateral relationship. It argues that the implementation and update of bilateral agreements has become too costly as a result of delays generated by domestic conflicts. Specifically, the EU has insisted on the creation of independent authorities for the settlement of disputes as well as mechanisms for updating bilateral agreements without having to resort to full-scale renegotiations. In November 2018, the negotiators on both sides finished their draft of an institutional agreement. However, it turned out that there is no majority for this agreement in parliament. The Federal Council started a consultation on the draft agreement. At the time of this writing (at the end of 2019), no solution is in sight. Policymakers have not pushed it, preferring to wait first for the outcome of the national election in November 2019 and then the outcome of a "limitation initiative" scheduled for May 2020 on curbs to EU migrants that has been proposed by the right-wing SVP. Meanwhile the EU has withdrawn its recognition of the Swiss stock market equivalence. In addition, negotiations about updating current and future bilateral agreement have basically stalled. Given the country's close integration with the EU market – accounting for 52% of Swiss exports and 70% of imports (2018) – Switzerland is highly dependent on a well-functioning relationship with this much larger economic partner. In contrast, the EU is much less dependent on Switzerland.

Broadly perceived as a laggard in the development of its welfare state, Switzerland caught up in the postwar period. Today it has a mature and generous welfare state. In a time of demographic change, this welfare state will only remain sustainable through high rates of economic growth. It is far from clear whether these high rates of growth can be realized in the future, in particular if the inflow of foreign labor from and trade with the EU is constrained.

Citation:
OECD 2019: Economic Survey Switzerland, November 2019, Paris: OECD

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Exporte Importe: https://www.eda.admin.ch/dam/dea/de/documents/faq/schweiz-eu-in-zahlen_de

United States

Score 8

The United States has maintained economic policies that have effectively promoted international competitiveness and economic growth. Compared with other developed democracies, the United States has generally featured low tax rates, less regulation, lower levels of unionization and greater openness to foreign trade. The country has enjoyed superior levels of growth, capital formation and competitiveness. The strong economic growth established during the Obama administration continued through Trump's first three years.

During Trump's first two years in office, Congress passed a major tax reform which included a tax cut for corporations and high-income individuals. Along with increases in defense spending and Trump's rejection of spending cuts for middle-class social benefits (Medicare and Social Security), the tax cut created a sharp increase in the already unsustainable long-term budget deficit. As of late 2019, the tax cuts were responsible for a roughly $500 billion increase in the annual federal budget deficit, which totaled more than $1 trillion.

During 2018, as the Federal Reserve (also known as "the Fed") began to raise interest rates, Trump repeatedly questioned the Fed's expertise and accused it of doing harm to the economy – which he felt undermined his political interests. And though he lacked the legal authority to do so, he threatened in 2019 to fire the Fed's chairman. Both Congress and financial markets ignored the apparent threat to the Fed's independence. The Fed lowered interest rates during 2019, accounting for signs of slowdown in the world economy.

Holding firm to his campaign claims that the United States has been treated unfairly in most of its trading relationships, Trump repeatedly attacked various foreign trade agreements throughout his first two years in office. This included the United States pulling out of the Trans-Pacific Partnership trade agreement. Trump also demanded that revisions be made to the North American Free-Trade Agreement with Canada and Mexico, after imposing major increases in tariffs affecting both countries. He has provoked a trade war with China, imposing major tariffs that China met with firm retaliatory measures, along with lesser conflicts with the European Union and Japan. In 2019, a new North American trade deal passed the House, and Trump announced a new trade deal with China. The Trump administration initiated massive subsidies to assist agricultural businesses severely hurt by the loss of exports to China.

Citation:
Jeff Stein, Trump's quest to shatter GOP economics reached its culmination in 2019, Washington Post, Dec. 27, 2019.

Austria

Score 7

The Austrian economic situation remains within the general European context, despite significantly greater political uncertainty. The former government, a coalition between the center-right ÖVP and the right-wing populist FPÖ, with a stable parliamentary majority, initiated some (neo-)liberal policies, such as a (comparatively) moderate liberalization of working time regulations. Those steps did not have much time to significantly impact on the country's economic performance before the center-right coalition collapsed in early summer 2019. Following the coalition's collapse, the current non-partisan government – appointed by the head of state and tolerated by parliament until a new government can be formed after the September 2019 elections – has not attempted to formulate any specific economic policies. The overall performance of the Austrian economy remains within the framework of the European Union – a course which can be described as stable.

Austria's economy can be seen as a relative success story, defined by moderate economic growth and social stability. The September 2019 elections have not yet resulted in a coalition agreement. However, as it seems clear that no coalition can be formed without the ÖVP, the new government will be led by the same party (and the same chancellor, Sebastian Kurz) as the previous one. The ÖVP's coalition partner may change, but the overall economic tendency will not, at least not significantly.

The outcomes of the previous government's policies did not have any visible impact on the overall consensus-oriented tradition of Austrian politics. This may change with a new government, especially as a new coalition partner will likely try to reformulate some of the former government's economic policies.

Chile

Score 7

Chile has an advanced macroeconomic and financial policy regime in place. This is rule-based and combines a floating exchange rate, inflation targeting, an autonomous central bank, an overall government budget rule, and effective regulation and supervision of banks and capital markets. As a result, macroeconomic performance has generally been quite satisfactory. A dominant economic role is assigned to foreign trade, markets and the private sector, complemented by active government regulation and policies aimed at limiting noncompetitive market conditions, extending social protection, and – to a limited degree – reducing poverty and income concentration. Economic legislation and regulation provide a level playing field for domestic and foreign competitors. Barriers to international trade and capital flows are negligible, and international competitiveness, adjusted for labor productivity, is relatively high. These policies have enabled a relatively high level of growth, and poverty rates have fallen substantially in the last few decades. Studies by Chile's central bank have revised forecast the overall economic growth rate for 2019 from an initial value of about 4% downward to between 2.5% and 2.75%. The International Monetary Fund forecasts subsequent growth rates of about 3% through 2024.

At about 7.2%, the unemployment rate showed no significant change in comparison to the last period under review. It thus remains at a relatively high level in comparison to the past 10 years.

At the same time, major structural weaknesses can be observed. Low labor productivity represents a persistent problem. This is especially the case in small and medium-sized businesses (SMBs), which are Chile's main employers. Low levels of labor productivity is – among other factors – connected to low average skill levels within the workforce. Minor education-sector reforms have focused on higher education, but given Chile's economic structure, there is a strong need to enhance capacities at a technical level. In the long run, deficiencies in the education system along with low investment rates in infrastructure and R&D will probably hinder economic growth and undermine the sustainability of the country's development path. The highly bureaucratic public administration is a further factor impairing productivity.

Economic stability and growth in Chile depend primarily on the export of commodities (e.g., copper as well as agricultural and silvicultural products) with relatively limited or no added value at all. Thus, this South American country shows a comparatively low level of industrialization; the manufacturing sector is small and the majority of consumer, intermediate and capital goods have to be imported. Chile is also highly dependent on energy imports.

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Informe Política Monetaria del Banco Central
http://www.bcentral.cl

http://www.bcentral.cl/web/guest/-/informe-de-politica-monetaria-septiembre-2018

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Estonia

Score 7

As an EU member state, Estonia forms its economic policy in accordance with EU strategies and has adopted a reform program, "Estonia 2020," that describes a set of objectives intended to improve the national economy's competitiveness. Its two central objectives are the increase of productivity and employment. The implementation of economic and innovation policy is the responsibility of the Ministry of Economic Affairs and Communications. In parallel, the Ministry of Education and Research develops and coordinates implementation of the national R&D strategy. These two strategies are supposed to be complementary but duplication and lack of synergy between ministries have been continuous problems. Similarly, labor policy falls under the purview of the Ministry of Economic Affairs, Ministry of Education and Ministry of Social Affairs. Due to growing labor shortages, the Ministry of Interior, responsible for immigration, has also become an important actor in economic policy.

The global economic climate has been mostly favorable in the period under review. This trend is echoed by the improved performance of the national economy. Yet, high tax rates on labor and strict immigration policies prevent Estonia from attracting the foreign labor urgently required due to Estonia's aging population.

France

Score 7

France's economic outlook is improving. Since President Macron's election in May 2017, he and his administration have launched an ambitious reform agenda. Over the past two years, an impressive set of reforms (probably comparable in magnitude only to the 1958 – 1959 reforms undertaken at the beginning of the Fifth Republic) have been adopted or launched. However, the Yellow Vest protests lasting from November 2018 through spring 2019 served to slow some reforms slightly, and forced the government to postpone green taxes on oil, abolish taxes and social contributions levied on overtime hours, and increase transfers to single parents and workers with low salaries or pensions. The overall costs of these measures, due both to lower fiscal receipts and higher expenses, has been estimated at €17 billion.

The 2020 draft budget proposes additional changes, such as a decrease in company taxes, an elimination of the local residence taxes (taxe d'habitation) for 80% of taxpayers (with a complete elimination by 2022), a substantial cut in social-system contributions paid by employees, and a total €5 billion decrease in the income taxes paid by low-income families. The overall objectives are to increase the net incomes of low-income employees and workers, prevent capital flight and increase incentives for investors. The crucial feature is the consistency of the overall package, which favors the creation of jobs, erases some defects of the current unemployment-benefit system, and bolsters company competitiveness while slightly increasing workers' incomes due to the reduction in social-system levies or contributions.

In the short run, the economic situation has remained relatively positive, although economic growth rates forecast for 2019 and 2020 have respectively been reduced to 1.4% and 1.3%. Business investment has been boosted by Macron's business-tax cuts, favorable financing conditions and increases in labor-market flexibility. Meanwhile, lower labor taxes and improved job training opportunities have helped boost job creation, although the high unemployment rate is declining slowly. The public deficit remains at its past level (98.8% of GNP), and is expected to decline by only 1% over the 2017 – 2022 period. While reductions in the overall budget deficit were originally planned, this will be actually higher (3.1% of GNP) in 2019 than in 2018, and the public deficit target set for 2020 (2.2%) may not be met. The deficit forecast for 2021 has been increased from 1.2% to 1.5%. The Social Security budget, which was supposed to be positively balanced in 2019, will in fact see a €4 billion deficit that is expected to be erased only by 2023. The financial consequences of Macron's social measures, announced on 10 December 2018 in order to calm the social unrest, have had both positive and negative effects. On the one hand, growth has been sustained due to the stimulus effect of spending measures; on the other, this has compromised efforts to balance the budget and reduce the public debt. However, given the situation at the time, there was probably no other politically acceptable alternative.

Citation:
OECD Economic Surveys, France, April 2019
https://www.oecd.org/economy/surveys/France-2019-OECD-economic-survey-overview.pdf

Germany

Score 7

Germany's economy avoided an outright recession, in 2019 but experienced a marked decline in its growth rate. In November, like many other institutions, the German Council of Economic Experts (Sachverständigenrat 2019) reduced its growth forecast, predicting that GDP would grow by 0.5% in 2019 and 0.9% in 2020 (after growth rates of above 1% in the preceding years). The weakening of international trade flows due to the trade dispute between the United States and China, and to other European and global uncertainties including the threat of a no-deal Brexit, has hit German export industries hard. Structural issues have further exacerbated these short-run cyclical factors. As of today, it is hard to predict how the country's vital car industry will cope with the technological transition to electromobility. Overall, the period's economic developments were split between the recessionary trends in the export industry and strength in the domestic economy driven by a continuation of the construction boom and high levels of private and government consumption.

Economic policy has continued to be rather passive. The crucial reforms still shaping labor-market institutions, unemployment benefits, the pension system, corporate taxation, the constitutional debt brake and liberalized labor migration from outside the EU are now a decade or more old. Although these reform packages of the 2000s improved Germany's competitiveness and increased its attractiveness as a destination for foreign investment, some of these advantages are gradually eroding. Within the field of corporate taxation, for instance, numerous tax reforms in important competing countries like the United States and France have left Germany as a relative high-tax location in comparison. What is also missing are convincing answers to the questions raised by demographic change and its consequences for the availability of skilled labor. The buoyant labor market has led to an increase in wages and a slight increase in unit labor costs, although this is not yet generally considered to be a threat to competitiveness.

There has been some activity aimed at improving the country's ability to meet the challenges of the digital transformation. In late 2018, the federal government adopted an Artificial Intelligence Strategy, with the goal of becoming a European or global leader in the development and practical use of AI technologies. This AI Strategy is intended to enhance research into artificial intelligence technologies, along with the subsequent development and implementation, thus strengthening the country's economic development and social cohesion and sustaining its high level of economic well-being.

Citation:
Sachverständigenrat zur Begutachtung der Gesamtwirtschaftlichen Entwicklung (2019): Jahresgutachten 2019/2020. https://www.sachverstaendigenrat-wirtschaft.de/jahresgutachten-2019.html
https://www.bundesregierung.de/breg-de/themen/digital-made-in-de/strategie-kuenstliche-intelligenz-ki–1546648

Iceland

Score 7

The economy has still not recovered fully from the harsh fiscal adjustment to the 2008 financial crash, which imposed a retrenchment equivalent to about 10% of GDP between 2010 and 2017. Public services, especially healthcare and education, have suffered a serious shortage of funds. Having run a small fiscal surplus in recent years, the central government now forecasts a deficit in 2019 due to lower tax revenue. Meanwhile, the central bank has lowered interest rates to counter a slowdown in economic activity due, among other things, to fewer tourist arrivals.

At 3%, inflation exceeded the official target of 2.5% in 2019 and may rise further as labor unions, under new leadership, continue to demand wage increases against the background of large wage hikes granted earlier by the Wage Council to members of parliament, senior public officials (and the president of Iceland who donated the salary increase awarded to him to charity). The salaries of members of parliament increased by 111% between 2011 and 2018. The Wage Council has since been disbanded. The council did not keep minutes of its meetings. Under these circumstances, and in view of ever higher CEO compensation, concerns about distributive justice in the labor market loom large.

The future of the banking sector remains uncertain. The government, which still owns two-thirds of banking sector assets in Iceland, has not yet presented any concrete plans for restructuring the banks. Iceland is one of very few countries in the world without any foreign competition in its domestic banking sector.

Iceland applied for EU membership in 2009. The preceding government had signaled its intention to abide by EU standards and to strengthen Iceland's institutional environment, including its regulatory policy. Due to disagreements between the government's coalition partners at that time, the application process was put on hold in January 2013. In 2013, a new government expressed its intention to unilaterally retract Iceland's membership application. A formal withdrawal was announced in the spring 2015. However, the European Union and the Icelandic government seem to disagree on whether this means that Iceland has fully withdrawn from the process. Specifically, the European Union has questioned the authority of Iceland's foreign minister to unilaterally withdraw an application approved by parliament. This question is most likely going to remain unanswered for some time.

Citation:
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International Monetary Fund (2018), Iceland: Staff Concluding Statement of the 2018 Article IV Mission, September 25, 2018.

Norway

Score 7

The economy is in a long-term transition. The long-term goal is to promote greater diversification, and to reduce dependence on oil and gas revenues. The rise in oil and gas prices after the dip in 2014/2015 has made the transition smoother, but also more protracted. There are growing concerns that rising housing prices and private debt levels will pose a challenge if interest rates increase.

The economy remains strong. Public finances remain solid, but high welfare costs represent a challenge in the long term. The country has long enjoyed strong economic growth and near-full employment and has benefited from a well-functioning system of tripartite cooperation.

The management of petroleum revenues – which are used domestically with prudence and otherwise invested abroad through a sovereign fund focused on equity, bonds and property assets – is held in high regard by international standards.

The state wields strong influence within the economy. About 40% of the equity on the Oslo stock exchange is under state ownership. Combined with the additional 30% under foreign ownership, this means that the share of the remaining indigenous private-capital sector is relatively small. When the state makes its investments, it most often does so on market terms. Economic policy is generally considered to be fair and transparent. Regulatory arrangements are generally seen to be sound.

The primary strength of Norway's economy lies in the public sector, particularly with respect to employment. The strongest areas are petroleum and petroleum-related industries such as maritime activities, as well as fisheries and fish-farming. It is a high-cost economy, both in terms of wages and taxes, and international competitiveness suffers in industries outside the petroleum sector. However, the high level of welfare benefits and high costs also represent challenges in a period of declining revenues from petroleum activities.

Although the country has managed its petroleum wealth responsibly, the economy is strongly petroleum-dependent and entrenched at a high-cost level, although costs have dropped significantly. Some observers are concerned that a lack of competitiveness in the mainland economy might pose a future challenge to maintaining the country's high standard of living and to expectations for continued high public-service standards. The downside of a petroleum-dominated economy, critics argue, is an economy that lacks entrepreneurship, is weak in terms of conventional industries and has less long-term strength than might be suggested by current favorable indicators. It also makes the economy vulnerable to changes in petroleum prices in world markets. These problems have now become strongly visible in the economy and a factor in economic policymaking.

Citation:
I see no sign that the economy has improved. Therefore I do not change the score.

Poland

Score 7

The Polish economy is still on a strong footing. Though real GDP growth declined slightly to 4.6% in 2019 from 5.1% in 2018, the economy has continued to grow well above the EU average. Boosted by a strong increase in social transfers, good labor market conditions, low lending rates and moderate inflation (2.3%), it is still largely driven by growth in personal consumption. Private investment growth strengthened in 2019, after several years of weak growth. Public investment has continued to grow, although at a slower pace. In August 2019, the government announced a new infrastructure program, which is supposed to modernize and expand the network of streets and highways, worth PLN 800 million. Whereas domestic investment has risen, net FDI relative to GDP dropped by 2.2 percentage points, reflecting the uncertainty over the PiS government's economic policy and violations of the rule of law. In most rankings of international competitiveness, Poland has lost ground. The strong growth in social spending has raised concerns about Poland's medium- and long-term fiscal stance, and ability to react to a possible economic downturn. As discussions about linking access to EU funds to rule of law indicators will continue, the government may have to adjust its economic policy, which relies heavily on the inflow of EU funds. Economic growth rates are also likely to suffer somewhat as a result of Brexit. Accounting for 6.4% of all exports, the United Kingdom is Poland's second-largest export market, while the second-largest portion of the remittances from Poles working abroad comes from the United Kingdom.

Citation:
Balcerowicz, L., A. Łaszek (2019): Poland's economic miracle won't last, in: Politico, October 10 (https://www.politico.eu/article/polands-economic-miracle-wont-last/).

European Commission (2020): Country Report Poland 2020. SWD (2020) 520 final. Brussels (https://ec.europa.eu/info/sites/info/files/file_import/2020-european-semester-country-report-poland_en.pdf).

Portugal

Score 7

In a country marked by considerable policy discontinuities across governments, the stability of the first Costa government, which governed until the October 2019 elections, helped foster and maintain a reasonably reliable economic environment.

The government maintained its strategy of gradually reversing previous austerity measures without generating adverse impacts on budgetary policy or the country's overall fiscal consolidation. It has also sought to facilitate investment through the SIMPLEX+ program, which aims to simplify bureaucratic processes.

The economy grew during the period under review. Following three years of economic downturn (2011 – 2013), 2018 marked the fifth consecutive year of economic growth – a pattern that has almost certainly been maintained in 2019.

Eurostat has provided a provisional annual growth rate of 2.4% for 2018, which is less than the 3.5% for 2017, but remains above the EU-28 and euro area averages – the second consecutive year in which the Portuguese economy grew faster than its counterparts. The estimated quarterly growth rate for the first two quarters of 2019 has also remained above the EU and euro area averages.

At the same time, there are some notes of caution. First, the estimate for 2019 points to a slight slowing down of economic growth, with the October 2019 forecast of the Portuguese central bank predicting a 2% growth rate in the current year.

Second, and most importantly, the Portuguese economy still faces a number of structural constraints that remained largely unaddressed by government during this period. A recent Bank of Portugal study on potential output (i.e., the highest total GDP that an economy could sustainably produce) found that Portugal's potential output has been decelerating since the 2000s and diverging from the euro area since 2003. The study concludes that "The results reinforce the case for structural reforms if policymakers desire to resume a sustainable economic convergence."

Finally, public and commercial debt is high, which should be addressed by the government.

Citation:
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Eurostat, "Gross domestic product, volumes: Percentage change q/q-4 (NSA)" available online at: https://ec.europa.eu/eurostat/tgm/refreshTableAction.do?tab=table&plugin=1&pcode=teina011&language=en

Eurostat, "Real GDP growth rate – volume: Percentage change on previous year" available online at: https://ec.europa.eu/eurostat/tgm/table.do?tab=table&init=1&language=en&pcode=tec00115&plugin=1

Spain

Score 7

Spain's economic situation remained stable in 2019. Spain's 1.9% economic growth rate for 2019 is higher than other large EU member states and the rest of southern Europe (aside from the tiny Mediterranean islands of Malta and Cyprus), but shows signs of slowdown. The recovery that began in 2014 has remained solid for six years in a row, consistently above the euro zone average, although this tendency has weakened toward the end of this period and, in particular, during 2019. In the context of domestic and international political and economic instability, growth is expected to decline to an annual rate of 1.5% in 2020 according to the European Commission.

Economic growth continues to be driven by private consumption, equipment investment and the positive contribution of net exports. However, the large stock of internal and external debt, both public and private, and high unemployment, in the context of weak productivity growth, are significant vulnerabilities. For its part, tourism, which is a key sector for the Spanish economy and employment, suffered an 1.3% fall in the number of foreign tourists visiting the country in July 2019 with respect to the same month in 2018 (according to data from the National Statistics Institute). This is the second consecutive year that the figure has fallen in the same period, mainly due to a decline in British and German visitors, and the competitiveness of other Mediterranean countries.

Citation:
European Commission (2019), Autumn 2019 Economic Forecast: A challenging road ahead, Spain
https://ec.europa.eu/economy_finance/forecasts/2019/autumn/ecfin_forecast_autumn_2019_es_en.pdf

September 2019, El Pais, Spain sees fall in July tourist visits for second year running, https://elpais.com/elpais/2019/09/02/inenglish/1567423811_074989.html

United Kingdom

Score 7

The UK economic framework was substantially reformed after 1979 in a market-friendly direction and most of these reforms were maintained after the election of the Labour government in 1997, albeit with some rebalancing toward labor interests – notably through the introduction of a minimum wage. The UK economy grew steadily from the early 1990s up to 2007, but then endured a deep recession during the financial crisis before recovering from 2013 onwards, despite weak demand from the euro zone, the United Kingdom’s largest export market. There are concerns that the economy is too reliant on consumers’ expenditure, fueled by overly high household debt and sustained by very loose monetary policy.

The change in government in 2010 led to the adoption of an economic policy framework ostensibly focused on budgetary consolidation, but there has been a substantial watering down of the fiscal rules put in place by previous governments; targets for returning to fiscal balance have repeatedly been pushed to later dates. This has meant the squeeze on public spending has been less than is often claimed because the government also chose to protect key areas of public services, such as healthcare spending. The corollary, especially as service charges on government debt increased, was that cuts in other areas of public spending had to be even deeper. Insufficient public investment is reflected in creaking infrastructure and skills shortages.

The economy initially appeared to shake off the political shock of the “leave” vote in the June 2016 EU referendum, with the fall in the exchange rate helping to absorb the shock. In 2017, however, economic growth slowed such that the United Kingdom shifted from being one of the most rapidly growing mature western economies to one of the slowest. The labor market has remained buoyant, with the employment rate rising to 75.9% in comparison to 75.7% in 2018, which was already the highest employment rate since the beginning of comparable estimations. This labor-market performance partly reflects a job-friendly economic policy. The average pay grew up by 3.7%, which is the highest growth rate since June 2008. Inflation is projected to remain stable around 2%. Moreover, disappointing productivity figures have led the independent Office of Budget Responsibility to reduce its estimate for the long-term growth potential of the economy and there is concern about how to boost productivity. The current account deficit exceeded 5% of GDP between 2013 and 2016, but decreased to 4.3% in 2018. In 2019, it increased slightly to 4.6%. This is indicative of the continuing export weakness of the UK economy. Uncertainty about future UK-EU relations and threats to the future access of UK financial services to the continental market are weighing on the economy.

Citation:
https://cdn.obr.uk/EFO_October-2018.pdf
https://www.bloomberg.com/news/articles/2018-09-28/u-k-current-account-deficit-widens-business- investment-falls

Australia

Score 6

Australia's economy weakened in 2019. While the country avoided slipping into recession, GDP growth per capita was -0.2% over the year to 30 June 2019, while unemployment edged up from a low of 5.0% in November 2018 to 5.3% in September 2019. Moreover, real household disposable income per capita has remained stagnant for a number of years, and as of mid-2019 was approximately 3% below its 2012 level. The economy has struggled to adapt to the end of the mining boom, when record-high commodity prices delivered substantial growth in national income. The decline in terms of trade has hit wages, and hence household incomes, hard. The end of the boom also saw a decline in tax revenue as a share of GDP, resulting in a succession of substantial budget deficits from 2009. However, tax revenue has picked up in the last two years, leading to forecasts of a budget surplus in 2019 – 2020, although this is unlikely to be realized if there is further weakening of the economy.

Australia's monetary policy is one of the country's economic bright spots. The Reserve Bank of Australia (RBA) has steered a convincing course between the ultra-loose policies of the European Central Bank (ECB) and the more sustainable approach of the U.S. Federal Reserve. The RBA has sought to prevent a sharp appreciation of the Australian dollar while also avoiding a situation in which it was providing liquidity too cheaply. It has been quite successful in recent years.

A lack of microeconomic and tax reforms over the last decade nonetheless continues to act as a drag on Australia's economic-growth prospects. The housing boom, which was a significant driver of economic growth for almost three decades, has come to an end. House prices in the major cities declined through mid-2019, falling approximately 10% in real terms from their June 2017 peak. Both the slowdown of the Chinese economy and the political conflict with China, which continued unabated in 2019, dampen the economy's future prospects.

The main barrier to integrated economic policy continues to be the federal structure of government, as well as the duplication of many services and regulatory functions between the federal government and the governments of the six states and two territories. The federal system has proven to be a barrier to achieving cooperation across jurisdictions. As a result, reform of many social services, most notably health and education, has reached an impasse. The core of the problem is the limited revenue-raising powers held by the states, which are dependent on block grants from the federal government. Prior to the 2016 meeting of the Council of Australian Governments (COAG), then Prime Minister Turnbull floated a proposal to reintroduce state income taxes as a way of eliminating the “vertical fiscal imbalance.” However, all but one of the state and territory leaders quickly rejected the proposal.

Belgium

Score 6

Located at the heart of the euro zone and the European Union, Belgium is a small, open and competitive economy. Its performance depends as much on the actions of its federal and local governments as on the general economic climate of the euro zone.

The high degree of exposure to global competition forces governments to keep an eye on the country’s international competitiveness, with mixed results. Belgium’s competitiveness eroded over the last decade, with production costs and market distortions progressively worsening in comparison with those of immediate neighbors. To compensate, the country offered increasingly generous tax deals to multinational enterprises. As these have recently been criticized as illegal state aid, the Michel government initiated a set of structural and tax reforms meant to 1) reduce the inflation gap (focusing more on wage-cost cuts than on product-market structural reforms), 2) partially remedy the labor-tax distortions that contribute to the competitiveness handicap and 3) reduce corporate taxation across the board – this latter policy being a recent development not initially planned by the government.

These efforts essentially represent the positive side of current efforts. On the negative side: public infrastructure investment remains low, as much as a full GDP point below levels in France and the Netherlands (see the World Economic Forum’s Global Competitiveness Report and the OECD’s economic survey of Belgium); employment rates remain consistently low (see the “Labor Markets” criterion); and the higher-education sector remains chronically underfunded, meaning that Belgium’s previously strong position in terms of worker skills is eroding.

Another major challenge hindering international competitiveness is the relatively low level of entrepreneurship, which hinders the market entry of young, innovative firms. In addition, the government is unusually right-wing for a country with a tradition of middle-of-the-road coalition governments. The previous government’s heavy-handed reform style has provoked substantial opposition and political unrest (e.g., demonstrations and strikes) that has done little to contribute to the investment climate. Last but not least, since December 2018, the federal government has in effect become a “caretaker” executive, preventing it to from acting proactively to improve the country’s international competitiveness.

Citation:
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Schwab, Klaus and Sala-i-Marti, Xavier (2017). The Global Competitiveness Report 2017–2018. World Economic Forum editor.

Productivity growth is slowing: http://www.oecd.org/global-forum-productivity/country-profiles/belgium.htm

Reforms and economic perspective: http://www.plan.be/admin/uploaded/201606211317350.FOR_MIDTERM_1621_11276_F.pdf

Too little entrepreneurship: http://www.plan.be/admin/uploaded/201606240814370.WP_1606.pdf

Bulgaria

Score 6

Since 2015, Bulgaria has maintained per capita economic growth rates in the range of 4% to 5%, with unemployment rates in 2019 at record-low levels since measurement started in 1991. In 2019, increasing exports contributed to a current account surplus, while the inflationary pressure noticeable in 2018 decreased. These positive developments have been countered by relatively low growth in real capital formation, lackluster performance within the industrial sector and rising expectations within the business community of a coming recession.

Economic performance has benefited from the stability of macroeconomic policy. The currency board, which has existed since 1997, has provided monetary stability, and fiscal policy has been sound. As for the microeconomic environment, businesses continue to complain about several problems that have not been adequately addressed by the government. One is the state of the judicial system, and the resulting uncertainty in the area of property rights and contracts. Another problem is the difficulty in dealing with the state due to rampant corruption and the unpredictable behavior of public administrators. A third is the lack of an adequate supply of qualified labor.

In the 2018 – 2019 period, Bulgaria underwent a strict review of its financial system by the European Central Bank (ECB), while the OCED reviewed the country's state-owned enterprise governance and insolvency framework. The checks were part of the requirements for Bulgaria to join the European Exchange Rate Mechanism II and the European banking union. While the results may be considered as generally positive, specific problems were identified with specific banks, and Bulgaria has not yet received approval to apply for membership in ERM2 and the banking union. Major outstanding questions for 2020 are whether this approval is issued, and whether the rising recessionary expectations will be fulfilled.

Citation:
European Commission (2020): Country Report Bulgaria 2020. SWD(2020) 501 final. Brussels (https://ec.europa.eu/info/sites/info/files/2020-european-semester-country-report-bulgaria-en.pdf).

Czechia

Score 6

The economic policies of successive Czech governments over the past 20 years have focused on achieving broad macroeconomic stability and attracting inward investment by multinational manufacturing companies drawn by wage levels about half the level of those in richer Western European neighbors. This strategy has ensured growth in most years; however, these growth rates have gradually slowed, in line with the trend in the euro area, the destination for a significant share of Czech exports. After strong GDP growth in 2017 (4.6%), growth slowed to 2.9% in 2018, with a forecast of 2.5% for 2019. Stagnating motor-vehicle exports, previously the main driver of growth, contributed in large part to the slower export growth. Thanks to rising pay levels, partly due to the pressure of low unemployment rates, growth has increasingly been supported by domestic demand. Wages were expected to rise faster than labor productivity in 2019 for the fourth year in a row. One serious long-term economic problem remains the character of the country's integration into global value chains. According to a study by Deloitte, the share of domestic value-added in total exports is an average of 61%, one of the lowest such shares worldwide, reflecting an economy based on the assembly of goods from imported parts and materials. More than 60% of Czech exports come from foreign companies. Compared to the preceding Sobotka government, the Babiš government has done less to drive advancement of the Czech economy by strengthening R&I.

Citation:
Deloitte (2019): Made in World. Analýza českého zahraničního obchodu a pozice v globálních hodnotových řetězcích. Prague.

New Zealand

Score 6

Similar to the previous National Party government (2008-2017), the current Labour-led government has pursued a cautious economic agenda, characterized by prudent fiscal policy despite increased welfare and health spending. Partly because of government prudence, but also because of tax receipts have exceeded expectations and the country's rail network has increased in value, New Zealand reported a budget surplus of NZD 7.5 billion for the year up to June 2019, up two billion dollars from the previous financial year. However, at the same time, the economy only grew by 2.1% – the slowest rate since 2013. While the export sector has continued to expand – driven largely by dairy products, the value of total goods exports hit a new record in March 2019 (up 19% from March 2018 to reach NZD 5.7 billion) – the manufacturing and construction sectors have been shrinking (by 0.2% in the quarter up to June 2019).

Business confidence has, according to ANZ's September Business Outlook Survey, fallen to the lowest levels since 2008. To some extent, the decline in business confidence is due to headwinds in the global economy – in particular, trade tensions between the United States and China as well as the unforeseeable impact of Brexit – and uncertainty surrounding socially progressive Labour policies, such as step-wise increases in the minimum wage rate and a ban on non-residents buying property. While evidence suggests that there is an element of political bias among those who complete the business surveys (Hickey 2017), the fall in confidence is also the result of some unpredictability in government decision-making, partly due to the coalition arrangements. For example, the government commissioned a review on a capital gains tax but, lacking support from New Zealand First, backed away from its recommendations and removed the proposal from the political agenda entirely, despite an expectation from Labour supporters that such a tax would eventuate. Other examples of government U-turns and policy changes include the decisions to drop a major road transport infrastructure project in the Auckland area (although additional funds have been put into other forms of transport), put a stop to oil and gas exploration in the Taranaki region, and replacing the KiwiBuild homeownership initiative – after having launched it only 18 months earlier.

Crucially, low business confidence appears to have contributed to weak investment. As per a report by the New Zealand Institute for Economic Research (NZIER) published in October 2019, investment in buildings, plants and machinery has dropped to the lowest levels in ten years. The OECD Economic Survey of New Zealand strikes an optimistic note, expecting business investment to pick up again in 2020. To help boost business investment, the Reserve Bank cut the official cash rate to a record low of 1% in August 2019.

Citation:
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Hickey, Bernard, 2017. ‘Politically-Biased Business confidence.’ Newsroom, 17 November. www.newsroom.co.nz/2017/11/17/61626/politically-biased-business-confidenceNZIER, Quarterly Survey of Business Opinion (https://nzier.org.nz/ABout%20QSBO/)
OECD, OECD Economic Surveys: New Zealand (http://www.oecd.org/economy/surveys/new-zealand-2019-OECD-economic-survey-overview.pdf)
Stats NZ, March exports hit a record $5.7 billion (https://www.stats.govt.nz/news/march-exports-hit-a-record-5-7-billion)
The Treasury, Budget 2019 (https://treasury.govt.nz/publications/budgets/budget-2019)
tradingeconomics.com/new-zealand/business-confidence

Slovakia

Score 6

After years of economic boom, Slovakia experienced an unexpected slowdown in economic growth in 2019. Real GDP growth fell from 4.0% in 2018 to about 2.3% in 2019, as slower economic growth in Germany and uncertainty produced by Brexit affected Slovakia’s export-oriented economy. In the second half of 2019, exports of goods, a strong pillar of the Slovak economy, declined.

The slowing of economic growth has revealed the risks and limits of Slovakia’s strategy of economic development with its strong reliance on the car industry and export performance. Future growth and prosperity will require strategic investment in education, innovation, infrastructure and energy technology. The Slovak business environment is slowly losing ground, as competitiveness is being undermined by high regulatory burdens, limited law enforcement, a lack of judicial and police independence, an unclear long-term economic vision, limited government responsiveness, low ICT adoption rates and a lack of innovation capability.

Citation:
European Commission (2020): Country Report Slovakia 2020. SWD(2020) 524 final, Brussels (https://ec.europa.eu/info/sites/info/files/file_import/2020-european-semester-country-report-slovakia_en_0.pdf).

OECD (2019): OECD Economic Surveys: Slovak Republic 2019. Paris.

Slovenia

Score 6

The Slovenian economy has been growing robustly since 2014. However, real GDP growth declined from more than 4% in 2017 and 2018 to about 2.5% in 2019, largely because of the high export propensity of the Slovenian economy and its strong dependence on development in larger European economies.

The Šarec government has stuck to the controversial infrastructure projects initiated by its predecessor, which include the construction of a second Karavanke highway tunnel toward Austria and the construction of a second railway line between Divača and the port of Koper. Both projects have continued to suffer from mismanagement, corruption and delays in implementation. Compared to its predecessor, the Šarec government has been more successful with the privatization of state banks, which has been on the agenda for some time. It sold 75% minus one share in the largest Slovenian bank (NLB) to institutional investors and the third largest bank (ABanka) to the U.S. fund Apollo, which owns Slovenia’s second largest bank, Nova KBM d.d.

South Korea

Score 6

South Korea’s economic growth has slowed since 2018 due to flagging exports and investments. Annual GDP growth was 2.7% in 2018, down 0.5 percentage points as compared to 2017. Korea also posted record current-account surpluses in 2018, signaling a high degree of international competitiveness. The Moon government’s cornerstone economic initiative is the “people-centered economy,” which focuses on job creation, income-driven growth and welfare expansion. Key initiatives include the transition of precarious job contracts into permanent positions and a gradual increase in the minimum wage. The minimum wage was increased by 10.9% in 2019. Following protest by business groups, President Moon promised to limit future minimum-wages. To stimulate the economy, the government has increased public investment, with the central bank supporting the fiscal expansion with interest rate cuts. The government has also promised to reform the country’s business environment by reforming the dominant business conglomerates (chaebol), although few concrete plans have emerged. At the time of writing, the primary focus was on “self-regulation” by the chaebol. Another promise to engage in deregulation has not yet had any tangible results. High levels of household debt remain a major economic problem, and the government has implemented various comparatively modest measures aimed at cooling down the real-estate sector. Unresolved trade conflicts with Japan and the United States, and continued trade conflicts with China sparked by the U.S. deployment of anti-ballistic missiles within South Korea represented the largest external challenges to the country’s economy at the end of 2019.

Citation:
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Croatia

Score 5

After six consecutive years of recession (2009 – 2014), the Croatian economy returned to growth in 2015. At about 3%, real GDP growth in 2019 was slightly higher than in 2018. After five years of economic recovery, real GDP finally returned to its level before the long recession. In 2019, the European Commission announced that Croatia no longer suffers from excessive macroeconomic imbalances, for the first time since the accession to the European Union in 2013. Fiscal balance and current account deficits have been replaced by surpluses.

The quality of macroeconomic policy has improved under the guidance of the European Semester process. Measures have been adopted to strengthen the institutional framework governing public finances and improve governance of state-owned enterprises. As for the professional management and privatization of state-owned enterprises, however, Croatia still lags behind.

The Croatian National Bank (HNB) has succeeded in keeping inflation in check. The private sector has benefited from ample liquidity and declining interest rates. However, policy toward the private sector has been derailed by the economic problems of Agrokor, the largest private company in Croatia and the Western Balkans. The company successfully reached an out-of-court settlement in July 2018, with two Russian banks (Sberbank and VTB banka) gaining the largest share of ownership (approximately 47%). However, the crisis was reignited in December

2019 when the Slovenian competition agency announced the seizure of one of Agrokor's prize assets, its shares in the Mercator retail group. Agrokor's management has described the action as a gross misuse of the law. In 2019, the number of newly formed enterprises for the first time dropped below 6,000.

Citation:
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Greece

Score 5

Compared to previous time periods, Greek economic policy during the period under review was relatively less restrained by externally imposed conditionalities. The three-year Third Economic Adjustment Program (supported by a €86 billion bailout) officially ended in August 2018. However, in view of the facts that 2019 was an election year, that – according to opinion polls – a government change was in sight, and that impediments to domestic and foreign improvement (excess and unpredictable taxation, government ambivalence regarding large-scale private investment) had not been overcome, economic policy did not substantively foster economic growth. As illustration, Greece's gross fixed capital formation in 2018 was 13% of GDP (the lowest such rate among the 41 OECD countries), while the country also ranked lowest among the OECD member countries with regard to potential output (IMF data).

However, there were signs of recovery. The Greek economy showed positive growth for a second year in a row (1.9% in 2018 and to 1.5% in 2017), and has caught up with the euro area's average rate (1.9%). Nevertheless, this remains a relatively low rate given the catch-up needs following the long economic crisis. Tourism was once again the main contributor to this growth. In 2018, Greece's tourism sector grew at 7% (almost three times the global average), and accounted for 21% of the country's GDP (global average: 10%).

The unemployment rate is slowly falling, though it remains close to 20% (it dropped from 25% in 2017 to 19.3% in 2018). The youth-unemployment rate is twice that. The labor supply has shrunk by nearly a half a million people, most of these being skilled workers who have left the country since 2010.

The government achieved a primary surplus in the 2018 budget, mainly by raising taxes and extending the lease of the Athens International Airport. In the period under review, economic policy remained constrained by the capital controls imposed by the Syriza-ANEL government in July 2015 with the aim of avoiding a bank run after the austerity-package referendum. However, the capital controls were finally lifted in September 2019. This development should boost economic activity, although the economy remains frail. In particular, there has been little progress in managing non-performing bank loans, which still constitute about 48% of all bank loans.

The Syriza-ANEL government continued its policy of imposing high taxes on income and assets while changing the details almost every year, creating an unstable tax environment. Increased taxation has helped achieve a state budget surplus, but has also acted as a disincentive to investment, thus contributing to the meager levels of economic growth in 2018 – 2019.

Prospects for future economic growth are better due to the government turnover of July 2019, which brought a more investment-friendly, single-party majority government to power, led by the New Democracy (ND) party. By late summer of 2019, the Eldorado Company, which had invested in a gold mine in Halkidiki (in northern Greece), and the Lamda Development Company, which had bought land in the former Hellenikon International Airport (to the south of Athens), witnessed progress in their cooperation with the newly elected government.

Substantial challenges remain, however. The banks' gross non-performing loans (NPLs) have fallen by a quarter since 2016, but still total €80 billion, or 45% of exposures. The country's external public debt remains at forbiddingly high levels (181% of GDP in 2018, by far the highest such levels in the EU). Almost 70% of this is owed to official European creditors, with some 70% of that owed to the European Financial Stability Facility. The IMF, along with most international observers, believes that this mountain of debt is unsustainable, and has called for deep relief. The country's creditors need to devise a plan for large-scale debt restructuring that may entail substantial losses for them. Finally, economic policy may become more fruitful if less pressure is exerted on private business and households to contribute to very high government-budget primary surpluses, like those achieved in the last several years. Although EU authorities refused to discuss such a prospect in the autumn of 2019, it is an issue that will probably surface again if Greece's creditors want to see the country attain much higher growth rates, and thus become better able to service its public debt.

Citation:
Data on Gross Fixed Capital Formation and potential output are drawn on IMF's world economic outlook for 2019 and is available on this SGI platform. GDP growth, unemployment and public debt are available from Eurostat.
On GDP: https://ec.europa.eu/eurostat/web/products-datasets/-/tec00115&lang=en
On unemployment: https://ec.europa.eu/eurostat/databrowser/view/tipsun20/default/table?lang=en
On public debt: https://ec.europa.eu/eurostat/web/products-datasets/-/teina230
Data on tourism is drawn on the World Travel and Tourism Council (WTTC), available at https://news.gtp.gr/2019/03/13/wttc-impressed-by-greek-tourism-sector-growth-rate/

Hungary

Score 5

The Hungarian economy has been growing strongly since 2014. In 2019, Hungary was one of the few countries to withstand the international slowdown in economic growth. Its real GDP growth rate of almost 5% was the highest in the European Union and OECD. Investment has risen to a record level, thanks to easy financing conditions, an expansionary fiscal policy and a large inflow of EU funds. However, the sustainability of economic growth looks doubtful, given the counterproductive streamlining of the education and R&I systems, growing labor shortages, and the state capture by the "(royal) court" (udvar) around Orbán. Hungary normally ranks last in business environment rankings among the Visegrád countries, and looks ill-prepared for Hungary's looming challenges (e.g., cuts in EU transfers), a global recession or structural problems in the car industry.

The challenges ahead have featured prominently in the open and sometimes impolite debate between the two economic policymakers of the Orbán regime. On one side, Mihály Varga, the Minister of Finance, has suggested a cautious approach with the accumulation of reserves for hard times. On the other side, György Matolcsy, the governor of the Hungarian National Bank, has nourished the dreams of a rapid catching up with the West – mentioning, as is usual in Hungary, Austria – by 2030 with the continued accelerated growth. In his speeches, Orbán has mentioned both scenarios alternatively – sometimes the cautious one warning about the coming global crisis, sometimes the optimistic one boasting that Hungary is the fastest developing country in the European Union and referring to the dreams presented by Matolcsy – in order to legitimize his regime.

Citation:
European Commission (2020): Country Report Hungary 2019. SWD(2020) 516 final, Brussels (https://ec.europa.eu/info/sites/info/files/2020-european-semester-country-report-hungary-en.pdf).

Japan

Score 5

Recent macroeconomic developments have been mixed. Japan has experienced an extremely long business-cycle upswing, lasting since late 2012. But growth rates have remained relatively modest, while structural constraints such as demographic conditions and labor-market rigidities continue to cast a shadow on future growth prospects. The real growth rate in 2018 was only 0.8% according to the IMF, down from 1.9% in 2017.

The policy goals of a 2% annual inflation rate and concomitant increases in inflation expectations remain elusive. The core annual inflation rate, excluding fresh food, stood at only 0.3% in September 2019. In mid-2019, the Bank of Japan trimmed its 2020 inflation target and hinted that it would not hesitate to take additional easing measures if the economic situation worsened. This signaled that existing measures were not considered sufficient, particularly if a global recession were to emerge.

Despite consistent government and central-bank activity, and despite the presence of significant corporate cash holdings deriving from retained profits, consumption and domestic investment rates remain sluggish. Compensating for the negative effects of an aging and shrinking workforce has proven to be extremely challenging. The initiation of the Comprehensive and Progressive Agreement for Trans- Pacific Partnership and the free-trade agreement with the EU in 2019, as well as the preparations for the 2020 Tokyo Olympic Games, may be interpreted as positive signals. However, the China-U.S. trade conflict and the increasing likelihood of a global recession are casting a shadow over future growth prospects.

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Mexico

Score 5

Economic and financial stability in the last decade represents a real achievement given the frequency and depth of macroeconomic crises in the 1980s and 1990s. The Finance Ministry and the central bank (Banco de México) benefit from a considerable wealth of technical expertise with many Mexican officials having internationally recognized qualifications in economics. In addition, the high rate of inflation, which was the second highest in the OECD in 2017 and 2018 due to various factors, dropped significantly in 2019.

Mexico has the OECD’s lowest tax-to-GDP ratio. For decades, the country’s low fiscal capacity was mitigated by oil revenues. The 2014 tax reform aimed to reduce the country’s dependency on oil revenues by cutting expenditures and raising non-oil revenues. The public debt anticipated in the reform, however, assumed an ambitious GDP growth rate, which did not materialize. Furthermore, the government assumed that an increase in oil prices would compensate for any revenues not collected. While this was a reasonable assumption at the time of the reform, it did not accomplish the goal of increasing fiscal autonomy from oil revenue. Nevertheless, the dept-to-GDP ratio decreased slowly from 56.76% in 2016 to 53.57% of GDP in 2018.

In comparison with most of the other OECD countries, Mexico’s GDP growth over the last decade has been rather slow. This situation – and national and international organizations’ downward revision of economic growth forecasts – was due to the fall in international oil prices and the increasing uncertainty over Mexico’s future of economic relations with the United States. In particular, the renegotiation of the NAFTA added major doubts to this difficult situation. These doubts were finally addressed when Mexico reached a trilateral agreement with the United States and Canada in the summer and fall of 2018. In June 2019, Mexico ratified the new trade agreement, the United States, Mexico and Canada Agreement (USMCA), which will replace NAFTA. However, the trade agreement will require major change, especially in the automotive sector, which is so important for Mexico. In the future, more automotive parts will be produced in the United States and wages in the sector in Mexico will increase.

In addition to the USMCA, Mexico renewed the free trade agreement with the European Union in 2018. This agreement guarantees, with a few exceptions, the free circulation of goods and services between Mexico and the European Union.

Already in February 2019, the new president, López Obrador, announced the founding of the Consejo para el Fomento a la Inversión, el Empleo y el Crecimiento Económico, which will act as a contact forum for entrepreneurs, government and civil society, and will discuss how Mexico can develop economically. López Obrador, who is a proponent of economic nationalism, has pledged to achieve an average growth rate of 4% in each year of his presidency until 2024. Despite this, in the first half of 2019, the Mexican economy grew at the slowest rate since 2009.

Despite ongoing reforms geared toward boosting productivity, the microeconomic picture is less positive. There is a lack of competition in key domestic economic sectors. Mexico remains a low-skilled, export-oriented economy tied to the U.S. market. The uneven distribution of income is among the worst in the OECD. High levels of corruption and violence are also severe impediments to inclusive economic development. Though the travel and tourism sectors, which account for 7.4% of the GDP, are growing, despite the high rate of violence in some parts of the country.

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Cyprus

Score 4

In 2019, Cyprus sustained strong growth and robust fiscal performance within an improved financial and economic environment. Nonetheless, reports by its creditors, the IMF, the ECB and the European Commission, as well as by other institutions stress that risks and weaknesses persist. Progress to improve the country’s low competitiveness rating remained marginal.

As an EU member with a strong services sector and favorable taxation system, Cyprus is attractive to investors . However, significant reforms are still needed to upgrade the country’s infrastructure, and improve its technological readiness, the education system and the overall legal environment.

The implementation of reforms as well as efforts to reestablish confidence and stabilize the financial system have yielded a scaled down financial sector governed by stricter rules. The banking sector is fragile and shrunk further as a result of the country’s former central bank, Cooperative Bank, defaulted on its debt in mid-2018. Having privatized some of its NPLs, the bank might benefit from new rules relating to NPLs.

Economic performance in 2019 continued to rely on traditional sectors which the EU and Cyprus Fiscal Council warn cannot guarantee long-term growth. Tourism, large construction projects and private consumption have driven growth; expected at around 2.9% in 2019, compared to 4.1% in 2018. While confident about the capacity of Cyprus to repay its debt, creditors added the new national healthcare scheme and the eventual disorderly hard Brexit as additional risks. They suggest that a stronger economy offers opportunities for long-due reforms. The IMF cites broader civil service and civil procedure reforms, privatizations and the introduction of an e-justice system as worthy policy objectives.

Though some NPLs have been removed from banks, very high ratios remain. Private and public debt could hamper bank access to sovereign markets. A large current account deficit and external financing needs make Cyprus vulnerable, but the improved composition of external liabilities and large gross external assets mitigates such risks according to the IMF.

Signs of improvement in the collaboration between the government and parliament in 2019 may benefit renewed efforts to promote reforms in the public sector. It is, however, too early to predict their outcome.

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Italy

Score 4

During the period under review, the first Giuseppe Conte government, supported by the Five Star Movement and the Northern League, held power until August, when the leader of the Northern League pulled his support and asked for a snap election. The parliamentary crisis was solved with a second Conte-led government, supported this time by the Five Stars, the Democratic Party and several smaller parties of the left and center. During the first Conte government, economic policy was the result of a continuous process of bargaining between the two parties, each of which were ready to increase expenditures and violate EU rules, and the much more prudent position of the technocratic finance minister (Giovanni Tria), who was quietly supported by the head of state. The Conte government had initially promised substantial changes in economic and social policies. The budget targets presented in autumn 2018, with the revised “Documento di Economia e Finanza” (NADEF), proposed a significant change in budgetary policies compared to previous governments, envisioning higher deficits for the next three years deriving from increases in social expenditures and pension costs coupled with tax reductions. The government’s declared goal was to fight poverty and provide a stronger stimulus for the economy, which had started to slow down in 2018. The two main measures introduced by the government (the citizen’s income and the reform of the pension law, with the so-called quota 100 that enabled earlier retirements) were presented as instruments for boosting a stagnating economy. In the end, however, after tough negotiations with the European Commission, the government accepted a reduction in its estimated budget deficit from 3% to 2.4%, and then finally to 2%. The expenditures for those measures had to be contained, while resources for public investment were cut; as a consequence, the economic policy’s stimulus force was almost completely lost. After the fall of the first Conte cabinet in August 2019, the second Conte government opted for a much more fiscally prudent economic policy, which was still being shaped in the final months of 2019. In both cases, however, the governments have failed to address the country’s economic problems with a serious economic vision.

Citation:
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Romania

Score 4

The Romanian economy continued to grow by about 4% in 2019. As in previous years, growth was stimulated by tax cuts and strong wage increases and is accompanied by high, and increasingly unsustainable, deficits in the fiscal balance and the current account. As a result of this economic overheating, Romania has one of the highest inflation rates in the EU. The country’s international competitiveness has been undermined by strong wage increases as well as skill and labor shortages, which has eroded investor confidence.

Citation:
European Commission (2020): Country Report Romania 2020. SWD(2020) 522 final. Brussels (https://ec.europa.eu/info/sites/info/files/2020-european-semester-country-report-romania-en.pdf).

Turkey

Score 4

Turkey’s most significant economic problems are related to external imbalances. At present, the country’s trade and current account balances, and currency and debt policies are unsustainable. Regarding trade and current account balances during the period under review, Turkey’s performance has been mixed. The current account deficit decreased substantially from $47.3 billion (5.6% of GDP) in 2017 to $27 billion (3.6% of GDP) in 2018. On a monthly basis, the current account averaged a $5.6 billion deficit between January and June 2018, but averaged a $1.9 billion surplus between August and November 2018. Despite the positive development in the current account balance, it is still difficult to argue that Turkey is on a healthy and sustainable economic growth trajectory. The turnaround has been largely due to the decline in imports that accompanied a slowdown in economic growth following the 2018 currency crisis.

As a result of decreasing confidence in the sustainability of Turkey’s external debt, foreign capital flows, which have been crucial to financing the country’s liquidity requirements, have dried up. Consequently, the government has been forced to recognize the country’s vulnerability to economic shocks, especially to currency shocks.

Turkey’s total gross external liabilities amounted to $596.2 billion, of which 75.8% were short-term liabilities, at the end of June 2019. The country’s net international investment position amounted to a net external debt of $351.5 billion. On the other hand, at the end of the second quarter of 2019, Turkey’s external debt amounted to $446.9 billion, with short-term debt accounting for 27.4% of total external debt.

According to Reuters, Turkey had to make $179 billion in external debt repayments over the 12 months to July 2019, with the private sector (especially banks) accounting for most of this debt. Turkey’s financing needs are substantial and access to international markets has become problematic. Subtracting the current account surplus of $4.4 billion over the 12 months to July 2019 from the $179 billion financing requirements leaves $174.6 billion, which is a very large funding gap for Turkey. The scale of this gap indicates that Turkey must make implausibly large policy adjustments in order to achieve a sustainable current account balance. As a result of recent developments, the prospect of an IMF bailout has increased considerably. However, the government has refused to ask for IMF support.

Turkey’s GDP increased by 7.5% in 2017 and 2.8% in 2018. According to the Turkish Ministry of the Treasury and Finance, GDP will grow by 0.5% during 2019.

According to the IMF, Turkey’s GDP declined from $852.6 billion in 2017 to $771.3 billion in 2018 and is expected to decline to $743.7 billion during 2019. Though, according to the Ministry of the Treasury and Finance, GDP is expected to decline from $789 billion in 2018 to $749 billion in 2019, before increasing to $812 billion in 2020. In contrast to developments in GDP, Turkey’s inflation rate (CPI), according to the IMF, is expected to decrease from 16.3% in 2018 to 15.7% in 2019. Meanwhile, the Ministry of the Treasury and Finance calculates that inflation will decrease from 16.4% in 2018 to 14.1% in 2019. The country’s annual inflation rate in September 2019 based on CPI was 9.26%, indicating that the headline inflation rate remains well above the central bank target of 5%.

In the case of monetary policy, on 13 September 2018, the central bank announced that bank funding provided through overnight lending will be provided via one-week repo auctions and that the policy rate would be increased from 17.75% to 24%. Thus, the central bank returned to a conventional monetary policy approach. The government was eager to see Turkey’s economy grow quickly following a period of recession in 2018 and wanted to revive the credit fueled expansionary policy seen in previous periods. In July 2019, the central bank governor was sacked after refusing to decrease the policy rate from 24%. The new governor has since slashed the central bank’s benchmark interest rates by 7.5 percentage points from 24% to 16.5%. As a result, the cost of borrowing from commercial banks has decreased significantly. Lending increased largely due to the country’s three state-owned banks, while private lenders have taken a more cautious approach, as the proportion of non-performing loans is increasing, and are advocating for debt restructuring.

On 30 September 2019, the government announced the New Economic Program 2020 – 2022, which aims to achieve a current account surplus of $1 billion (0.1% of GDP) in 2019 and a further $9.6 billion (1.2% of GDP) in 2020.

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