



REFORM BAROMETER 2019

BUILDING AN EU FOR EUROPEAN
BUSINESSES TO SUCCEED GLOBALLY





WHO ARE WE ?



BusinessEurope is the leading advocate for growth and competitiveness at the European level, standing up for companies across the continent and campaigning on the issues that most influence their performance.

A recognised social partner, we speak for all-sized enterprises in 35 European countries whose national business federations are our direct members.



WHAT IS THE REFORM BAROMETER ?



BusinessEurope's Reform Barometer looks at the global competitiveness performance of Europe on the basis of key indicators covering taxation and public finances, business environment, innovation and skills, access to finance and financial stability, and labour market. Based on a survey of BusinessEurope's member federations, the report evaluates the recommendations for structural reforms made under the European Semester, assesses progress in implementing them and identifies priorities for future reforms.

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FOREWORD



With growth of around 2% and over 1 million jobs likely to have been created, 2018 can in many respects still be seen as a strong year for the EU economy. Across the EU, businesses continue to innovate and export world-leading products, creating jobs and wealth for communities.

The purpose of our Reform Barometer is to look behind the headline numbers to get a full picture of prospects for the EU economy. This means recognising that after a break of 2 years, for the 7th time in the last 10, US growth once again exceeded that of the EU. And whilst the US economy is benefitting from a significant pro-cyclical fiscal stimulus, the EU has more to do to return to a normal monetary policy stance. Similarly, unemployment at 6.9% remains too high, particularly in several member states where it exceeds 10%. Moreover, in part due to continuing global trade tensions, there were clear signs during the final months of 2018 that the recovery is slowing, with forecasters generally expecting EU growth in 2019 to be around 0.5% lower than had been expected last summer.

But rather than fixing the roof whilst the sun continues to shine through growth-enhancing reforms, our survey suggests governments have failed to step up their reform efforts. Our member federations consider that member states have satisfactorily implemented only 20% of the essential reforms agreed with the EU. Whilst the politics of reform can often be challenging, governments should keep in mind recent work from the ECB, for example, which suggests that sound structural

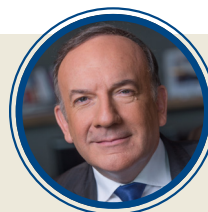
reforms could reduce the probability of a severe recession by around 20%.

Our special section this year looks at Europe's performance in developing high-growth, world-leading firms. A 25-year comparison of the 10 largest global firms reminds us of the rapid changes we are seeing in the global economy and broader society, both with the opening of emerging markets and the innovation and exploitation of, particularly, digital technologies.

Our analysis shows that whilst the EU retains many world-leading firms, we have fallen behind in our capacity to start and develop global companies. For example, none of the 10 largest companies by market value are currently from the EU, whilst the EU is home to a declining proportion of the world's most profitable firms.

As Europe develops new priorities for a new political cycle, we should reaffirm our commitment to making our continent the best place to start and grow a business. Ensuring we support companies in their efforts to invest, innovate, and create jobs and prosperity means increasing our reform efforts to improve the business environment, upgrade our skill and technological capabilities and ensure our labour market regulations support job creation.

Pierre Gattaz
President



Markus J. Beyrer
Director General



EXECUTIVE SUMMARY

PART 1: EU COMPETITIVENESS IN THE GLOBAL ECONOMY



2018 saw a slight moderation of EU economic growth to an estimated 2.1%, compared to 2.4% in 2017. But with growth of 2.9% in the USA in 2018, EU growth has now been lower than US growth for 7 of the last 10 years.

While around 1 million jobs were created in the EU during 2018, with unemployment falling from an average of 7.6% in 2017 to 6.9% in 2018, the EU's unemployment rate remains well above the 3.9% in the USA in 2018.



This year's barometer shows in particular that the EU is losing ground in terms of developing world-leading companies. For example, none of the top 10 global companies by market capitalisation is based in the EU.

When considering the most profitable global firms, we see that the global share of 'superstar' firms in Europe declined over the last two decades (while Western Europe hosted 36% of the top 10% of global firms by economic profits in the mid-1990s, its share has dropped to around 25% in recent years).





1. BUSINESS ENVIRONMENT

- It is significantly **more expensive to start and very difficult to grow a business in the EU** compared to the USA.

POLICY RECOMMENDATIONS



- 1** Further integrate markets for goods and services, including logistics and network services, and ensure a barrier-free framework that helps wide-scale roll-out of digital technologies.
- 2** Ensure that regulation, at EU and national level, follows the better regulation principles and is properly enforced, with a minimum of administrative burdens in order to support business start-ups and companies' expansion. Competitiveness proofing, including an SME test, must be an integral part of the ex-ante impact assessment for all legislative proposals and independent scrutiny of impact assessments must be reinforced.
- 3** Energy prices must allow EU businesses to be competitive on international markets. Targeted measures (e.g. reforming taxes and levies, liberalising energy markets, etc.) to address the energy price differential with major competitors and to ensure energy security should be introduced.
- 4** Trans-European (and national) infrastructure must be significantly improved and expanded. Remaining regulatory, administrative and technical barriers need to be removed to ensure necessary access to infrastructure facilities, inter-connections, inter-operability and to create an investment-conducive regulatory and financial framework.

2. INNOVATION AND DIGITAL TRANSFORMATION

- **EU R&D intensity** is much lower in the EU (2.0% in 2016) than in Japan (3.2%) and the USA (2.7%), and is also reflected in the low number of patent applications. China significantly increased its share of spending over the last decade (from 1.4% to 2.1%) and has also overtaken the EU.
- The EU continues to lag behind its competitors in some **key metrics for digital communication**. In particular, (fast) fibre connections are much less prevalent in the EU, compared to the leading countries Japan and South Korea.
- Europe has a strong record in producing robots, particularly for industrial applications, yet this is not matched by our ability to deploy the robots with the EU using fewer robots per employee than our competitors in South Korea, Japan and the USA.





POLICY RECOMMENDATIONS

- 1** EU member states should increase R&D spending and support stronger private-sector R&D investment, in order to reach the EU's 3% target. The post-2020 EU budget (MFF) must scale up R&D and innovation support.
- 2** More business-oriented innovation policies can ensure a greater economic impact from investment in research and innovation. Targeted initiatives must stimulate private R&D investment and incentives for cooperation between companies and research institutes in networks and clusters should be improved in order to facilitate the commercialisation of innovation. Regulation excessively focused on precaution and risk avoidance will stifle investment in innovation.
- 3** A strengthened digital infrastructure is essential for the EU to adopt the latest technologies enabling businesses to compete globally. This is especially the case when it comes to providing very high-capacity networks in order to launch 5G on a large scale.
- 4** Ensuring a digital transformation will require a fully functioning integrated digital single market. As well as network investment, action is needed to ensure a barrier-free level playing field for cross-border e-commerce, prevent forced data localisation measures, and to address tried and tested, fit-for-purpose frameworks in the areas of consumer legislation, copyright and data protection rules.
- 5** Europe needs to improve its cybersecurity; it currently invests less in this area than other regions, and as a consequence is slower to respond to threats, increasing uncertainty for business.

3. LABOUR MARKET AND SKILLS

- Whilst more than 13 million jobs have been created since the peak of the euro crisis in 2013, the **EU unemployment rate** (6.7% in November 2018) remains well above that in the USA (3.7% in November 2018).
- Even though unemployment rates are still too high in many member states, businesses increasingly report difficulties in **hiring qualified workers**.
- Comparing PISA 2006 and 2015 outcomes suggests that the EU has made little progress in closing the **structural difference in education performance** with Japan, Canada and South Korea.
- The **average tax wedge** is in Europe with 41.5% almost one-third higher than in Japan and the USA (both about 32%).



POLICY RECOMMENDATIONS



- 1** Urgent policy action is required to avoid labour market mismatches increasingly acting as a break on economic growth. Education and training systems need to be better tailored to labour market needs, particularly with more STEM graduates (science, technology, engineering and maths). An important priority is to achieve well-functioning apprenticeship systems across Europe. This amongst others means progressing towards a majority of the apprentices' training time taking place in the company. Policy benchmarking and a better use of the European Social Fund is needed to support Member States' reform efforts.
- 2** Improve employment incentives through cuts to tax wedges (non-wage labour costs), particularly for low-income workers, including through lower social security contributions and/or other tax incentives to make work pay, ensuring that taxation does not form a disincentive to work. Open, dynamic and mobile labour markets are needed to support new and more diverse career paths and smooth transitions between jobs, sectors and employment statuses. These more diversified careers need to be accompanied by adequate social security systems promoting professional activity.
- 3** In order to increase global competitiveness, the labour market regulatory framework needs to be clear, simple and flexible. Increases in labour costs must be consistent with rises in productivity growth. This means putting in place policies that can raise long-term productivity.
- 4** Set in motion a genuine partnership for labour market reforms: Rather than trying to solve labour market challenges across the board at European level, the European Union's primary role is to provide information, incentives and know-how for member states and social partners to design, implement and evaluate policies addressing the structural labour market challenges they face.
- 5** To mitigate negative impacts of population ageing, reforms must encourage people to stay in the workforce longer, make pension systems sustainable, and integrate legal migrants into the workforce. In order to make social protection systems more effective, social investments should be focused on areas where they can enhance growth (e.g. skills development, childcare), with the right balance found between adequacy and sustainability of social safety nets.

4. ACCESS TO FINANCE AND FINANCIAL STABILITY

- While the Euro-area as a whole has made progress in reducing **non-performing loans (NPLs)** since 2012, NPLs were 3.4% of GDP in 2017, still well above the 1.1%-1.2% seen in the USA and Japan.



- Euro-area businesses fund themselves to a larger extent via **bank lending** compared to the USA, where companies rely more on **capital markets**. Stock market capitalisation (as % of GDP) in the Euro-area is less than half that in the USA.
- The gap in terms of **venture capital funding** with the US has increased in recent years. \$19 bn were invested in the EU in 2018, compared to \$86 bn in the USA.
- Whilst **Euro-area banks** now feel more confident in **lending** again outside of the EU, their lending to other banks, institutions and firms within the Euro-area, but outside of their own member state has fallen strongly in recent years, despite the first steps being put in place to complete the banking union.



POLICY RECOMMENDATIONS

- 1 Particularly in light of the UK leaving the EU, reinforce and implement the Capital Markets Union to ensure that the EU puts in place a genuine single market in financial services, and develops complementary sources of finance to bank lending.
- 2 Take action to ensure prudential rules strike the right balance between increasing financial stability and supporting companies' financing needs for investment and business activities.
- 3 A full banking union must be put in place, with rapid agreement and implementation of an EU deposit insurance scheme, alongside the existing supervision and resolution pillars, needed to address the continued fragmentation of EU savings and credit markets. However, further asset quality reviews of all banks are necessary before establishing a common system.
- 4 Address still high levels of NPLs in many European banks in a way which increases new lending and maintains financial stability.

5. TAXATION AND PUBLIC FINANCE

- Much more remains to be done to reduce EU **public debt** levels which at 81% of GDP are still well above the 60% Maastricht limit.
- **Public expenditure** in the EU is 45% of GDP, well above levels in Japan (37%) and the USA (36%).
- The share of **growth-friendly public spending** in overall spending is just 30.9% in the EU, compared to 44.9% in the USA.



POLICY RECOMMENDATIONS



- 1** In all member states, there is scope for making public finances growth-friendlier and more efficient, in particular by targeted reductions in non-productive public spending and by reductions in distortionary taxes that hamper growth.
- 2** Proper implementation of the Stability and Growth Pact (SGP), drawing on built-in flexibility, remains essential to help member states put their public finances on a sustainable footing. This is key in order to strengthen investors' trust in the Euro-area. But it is also essential that the SGP gives the fullest possible support to member states who wish to orientate their budgets towards investment and growth-supporting expenditure.
- 3** Tax reforms should reduce taxation on labour and capital, including corporation tax, which are particularly damaging to growth and employment.
- 4** Member states should continue their efforts to ensure the administration of their tax systems becomes simpler, more transparent and user-friendly.

PART 2: STRUCTURAL REFORM PROGRESS - MEMBER FEDERATIONS ASSESSMENT

- While our member federations believe that the EU country-specific reform recommendations (CSRs) focus on the right reform objective, member states still demonstrate **unsatisfactory levels of implementation**. Only 20% of the CSRs assessed have been implemented appropriately according to our members, a slight decrease compared to our previous assessment.
- The most pressing concern for our members remains the **slow pace of reform on the labour market**. In particular, measures to improve labour market mobility can help ensure that workers are able to maximise the use of their training and specialist skills in their jobs. Furthermore, members are increasingly concerned about the slow pace of reform in wage-bargaining and wage-setting policies.



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PART 1: EU COMPETITIVENESS IN THE GLOBAL ECONOMY

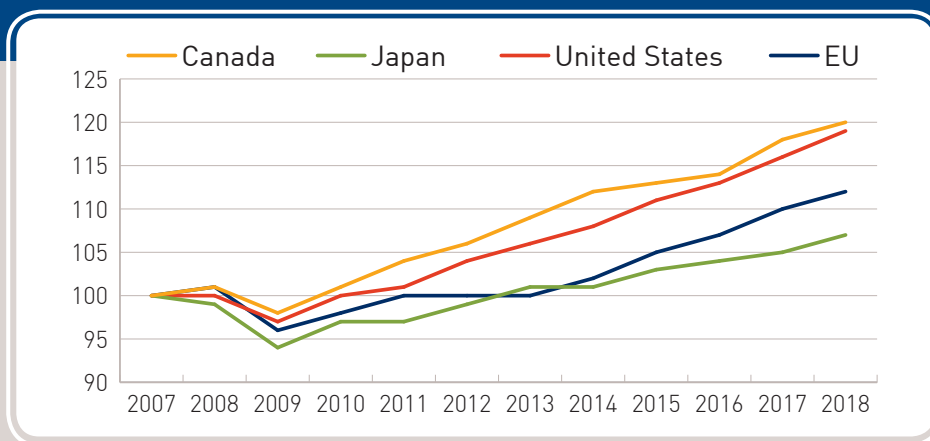
INTRODUCTION

Despite strong recent growth, the EU needs to improve its overall global competitive position

2018 saw a slight moderation of EU economic growth to an estimated 2.1%, which compares to the strong 2.9% growth recorded in the USA. While around 1 million jobs were created in the EU during 2018, with unemployment falling from an average 7.6% in 2017 to 6.9% in 2018, the EU unemployment rate remains well above the 3.9% in the USA in 2018.

As a consequence of growth in the EU being lower than US growth for 7 of the last 10 years, a clear growth gap has emerged (graph 1). EU output was only 12% above its 2007 pre-crisis levels in 2018, compared to 19% and 20% in the USA and Canada respectively.

Graph 1: The EU economy has grown less than the US since the crisis



Real GDP, constant prices
and national currency,
2007-2018

Source: BusinessEurope
calculations based on
IMF data

Moreover, it is also clear that the strengthening of the EU's recovery in recent years is underpinned by a number of temporary factors, notably the ECB's expanded asset purchase programme. A key question is thus which possible long-term impact the expected reduction in ECB monetary stimulus will have.

¹ Down from strong EU growth of 2.4% in 2017.

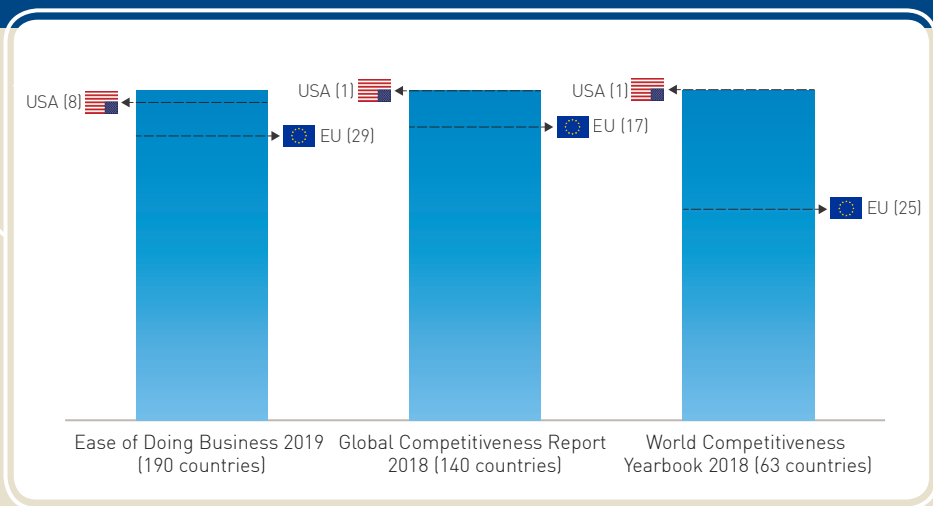
Overall, independent studies give a useful summary overview of the EU's competitive position in the global economy. As shown in graph 2, competitiveness and ease of doing business rankings all indicate that the competitive position of the US economy is well above that of the EU. While the USA ranks twice 1st place and once 8th place in the global rankings, the EU comes out only as 17th, 25th and 29th (weighted average of EU countries, where the individual performance strongly varies).

Graph 2: Major global competitiveness rankings all place the EU well below the USA

Global competitiveness & ease of doing business rankings

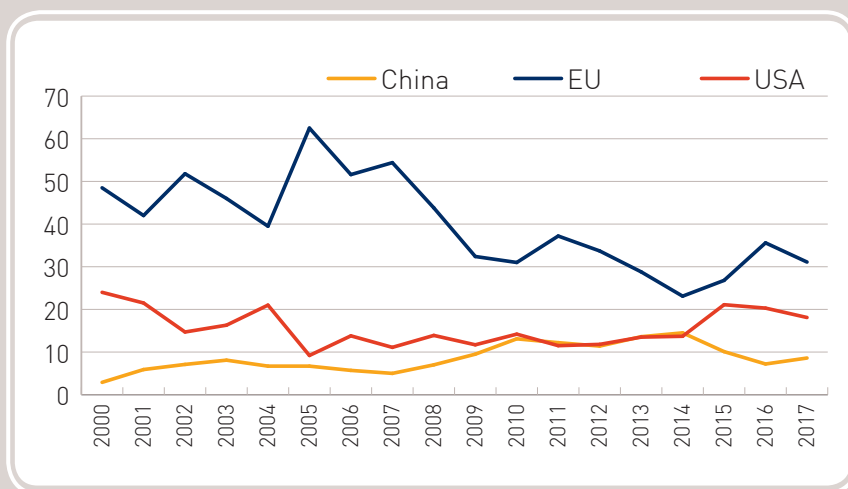
Notes: Weighted average of EU countries

Source: World Bank Group, World Economic Forum and International Institute for Management Development (IMD)



Furthermore, foreign direct investment (FDI) inflows also provide an indicator of how attractive foreign companies find the EU as an investment destination. While the EU remains the largest global recipient of foreign direct investment inflows as shown in graph 3, its importance has fallen over the last decade, with its share of global FDI inflows dropping from 54% in 2007 to 31% in 2017. Whilst this fall occurred largely in the period up to 2014, there are recent signs of stabilisation.

Graph 3: The EU's share of global FDI inflows has fallen by two fifths between 2000-2017



Foreign direct investment, net inflows in the EU, China and USA as % of global inflows, 2007-2017

Source: BusinessEurope calculations based on World Bank data

Finally, as shown in detail in our in-depth analysis in box 1, one worrying trend is that the EU is losing ground in terms of the largest companies. For example, 8 of the top 10 global companies by market capitalisation are based in the USA and 2 in East Asia, with none in the EU. Of the top 10% of global firms by economic profits, Europe hosts only 24%, compared to 38% in the USA and Canada combined, with the EU's share falling particularly strongly over the last two decades.

Against this background, our report looks into the underlying strength of the EU economy, and in particular the extent to which EU member states have been undertaking the necessary structural reforms to secure growth in the long term, once temporary support subsidies.

- The **first chapter** considers how the EU compares to our major competitors in a number of key areas (the overall business environment, particularly around innovation and digitalisation, labour market and skills, access to finance and financial stability, and taxation and public finances) crucial to businesses being able to provide the platform for growth, prosperity and employment creation.
- The **second chapter** considers the recent record, as judged by businesses in our member federations across the EU, of member states implementing the key economic reforms agreed with the European Commission and Council as part of the European Semester process.

BOX 1 Significant high-growth firms – How is the EU performing?

One indicator of the pace of change in recent years in the global economy is the significant change in the list of the world's largest companies. As the table below shows, 4 of the 6 largest companies in the world according to market value have been founded within the last 25 years, with the remaining 2 founded within the last 50. By comparison if we were to look at the 10 largest companies in 1990, just one would have been founded within the preceding 25 years. A key factor behind such relatively rapid change is clearly digitalisation, with each of the largest 6 companies having a strong digital foundation.

Ensuring that the EU is able to develop and grow world-leading companies is a key challenge, not the least because research suggests that the world's leading firms (as measured by profitability) are increasingly likely to have significantly higher productivity and profitability than average firms and are likely to be disproportionately larger investors in R&D, as well as often being seen amongst employees as the most satisfying companies to work for.

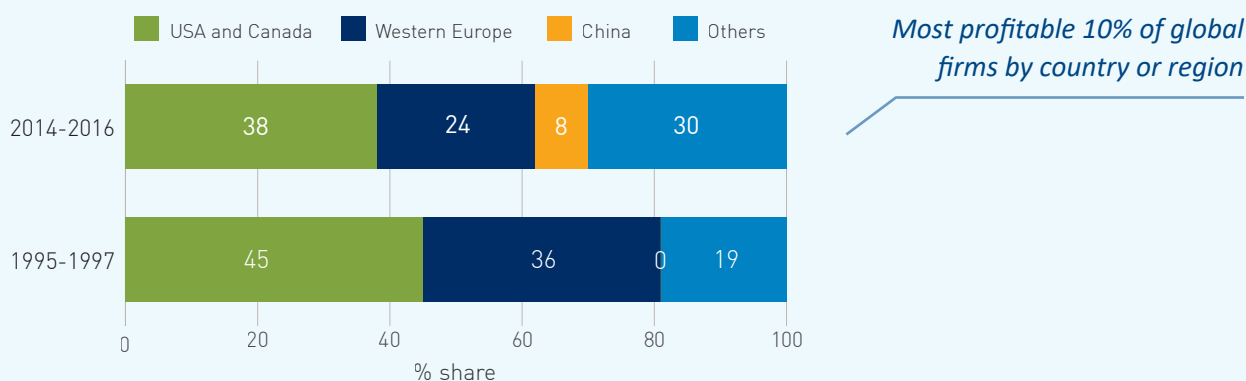
However, a look at the top 10 global companies underlines the fact that the EU faces challenges in developing such world leading companies (table 1). Eight of the top 10 global companies by market capitalisation are based in the USA, with two in East Asia, but none in the EU.

Rank	Company	Country	Market value (billion)	Founded
1	Apple	USA	\$926.9	1976
2	Amazon.com	USA	\$777.8	1994
3	Alphabet	USA	\$766.4	2015
4	Microsoft	USA	\$750.6	1975
5	Facebook	USA	\$541.5	2004
6	Alibaba	China	\$499.4	1999
7	JPMorgan Chase	USA	\$387.7	1968
8	ExxonMobil	USA	\$344.1	1859
9	Johnson & Johnson	USA	\$341.3	1886
10	Samsung Electronics	South Korea	\$325.9	1969

Source: BusinessEurope staff calculations

It is a similar story if we consider the EU in terms of the most profitable global firms. According to McKinsey, while Western Europe hosted 36% of the top 10% of global firms by economic profits in the mid-1990s, its share has dropped to around 25% in recent years (graph 4). In contrast, the decline in the combined global share of the USA and Canada has been much less dramatic (-7 pp, compared to -12 pp in Western Europe), with North America still accounting for 38% of such firms.

Graph 4: The global share of 'superstar' firms in Europe declined over the last two decades



Source: McKinsey, BusinessEurope staff calculations

Whilst we would like to make a full comparison of the EU's performance in developing high-growth firms of all sizes, such a comparison is difficult given the different global definitions for such enterprises. In particular, the OECD uses a much narrower definition for US than for EU firms: While EU high-growth firms are defined as enterprises with average annualised growth in the number of employees of more than 10% per year over a three-year period, in line with the European Commission's own definition, a 20% per year growth rate is used for US firms³.

Nevertheless, despite this much more restrictive definition for US firms, it is striking that OECD data shows that high-growth companies in the USA still employ almost as many people as those in the EU (23 vs. 27 employees per million citizens).

'Unicorn' firms are less frequent in the EU and on average less valuable

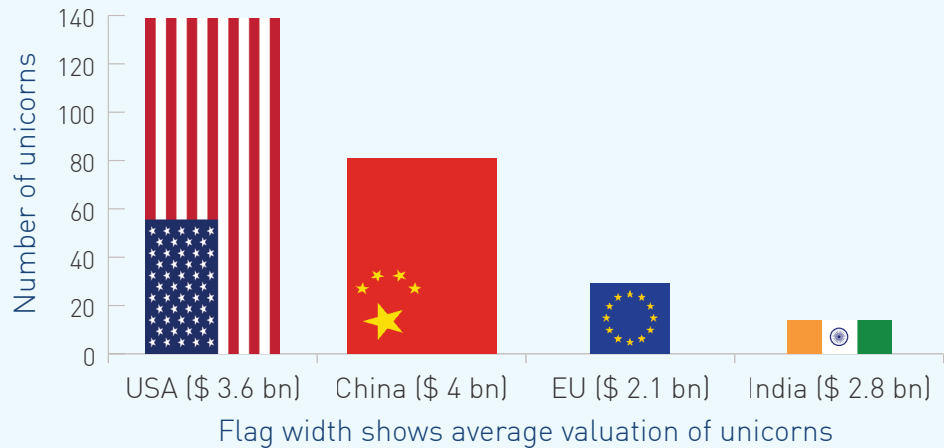
More comparable data is available as regards high-growth firms that have reached a \$1 billion-dollar market value within a short time-frame from start-up, the so-called 'unicorns'.

As shown in graph 5, the EU has not matched other regions when it comes to developing such firms, with the number of unicorns founded since 2010 amounting to only 29 in the EU, compared to 139 in the USA and 81 in China. Moreover, the average value of EU unicorn firms is \$ 2.1 billion US dollars, only about half that in China (\$4 bn) and the USA (\$3.6 bn). This again illustrates the challenges that the EU has with scaling up such enterprises.

²Discussion paper McKinsey Global Institute, "Superstars: The dynamics of firms, sectors, and cities leading the global economy", October 2018. The paper looks at 6,000 of the world's largest public and private companies, each with an annual revenue greater than \$1 billion.

³ In both cases, the enterprise in question must have ten or more employees at the beginning of the period.

Graph 5: Number and average value of unicorns by region

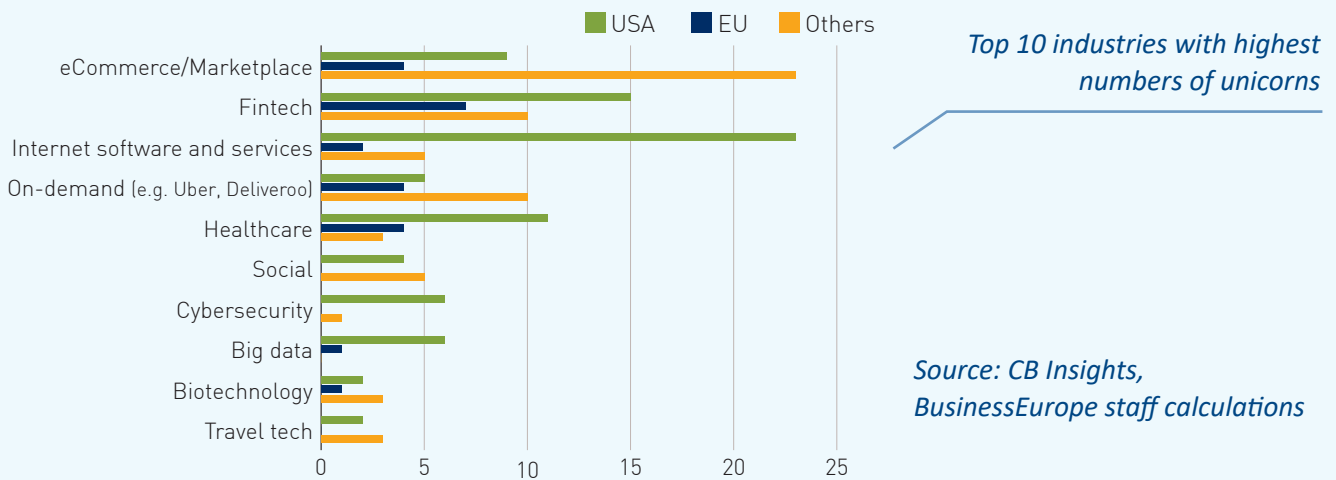


Data until November 2018
Source: CB Insights,
BusinessEurope staff calculations

The high concentration of unicorns in the digital economy is illustrated in graph 6, with high numbers of unicorns having been founded globally in sectors such as e-commerce, internet software and services, FinTech and on-demand services.

Chart 6 also provides an indication of the EU relative strengths as a base for the growth of unicorn firms. While the EU lags behind in all of the largest sectors, it performs less badly in the areas of FinTech, on-demand services and healthcare.

Graph 6: Most unicorns can be found in sectors related to the digital economy



Top 10 industries with highest numbers of unicorns

Source: CB Insights,
BusinessEurope staff calculations

How can the EU develop more world-leading firms?

The fact that EU has not been able to develop more world-leading firms in recent years is likely to arise from a number of inter-related factors. Improving policies in the following areas can play a particular role in enabling the creation and expansion of high-growth businesses in the EU:

- **A supportive business environment** is crucial for providing a basis for the creation and expansion of firms, particularly when young entrepreneurs are increasingly able to choose where in the world to locate their activity. The EU ranks only 53rd on average in terms of the ease of starting



a business according to the World Bank, and only 29th on average in terms of the overall ease of doing business (compared to 8th for the USA). As well as reducing administrative burdens for business, **completion of the digital single market** is essential to help provide the domestic base from which new companies can develop economies of scale and compete globally.

- **Innovation and skills** are key to ensuring that companies have the competitive advantage to attract customers and grow. Key weaknesses in this area are highlighted by low R&D intensity (2.0% of GDP in 2016 compared to 3.3% in Japan and 2.8% in the USA) and increasing skills shortages, particularly in science and technology. As well as promoting innovation and skill development, **policies to better link companies, research institutes and education, and create clusters of knowledge and competence, can be catalysts for business growth.**
- **Access to finance** is crucial for starting and expanding high-growth firms. The EU lacks the variety of financial support channels which US companies enjoy. The EU's share of global venture capital is just 12%, compared with 55% for the US whilst capital markets, crucial for further expansion are similarly much less developed in the EU. **As well as improving EU venture capital provision, reinforcing and implementing the European Commission's Capital Markets Union proposals can be an important driver of business expansion.**
- Consider the implications of changes in the global economy when implementing EU **competition policy**. A strong European competition policy is crucial for the well-functioning of the Single Market but it might be necessary to re-assess the European approach to company size in order to avoid unnecessarily preventing the emergence of sizeable European companies able to compete with global enterprises operating by different rules.

I. BUSINESS ENVIRONMENT

KEY OBSERVATIONS

- ▶ It is significantly more expensive to start and very difficult to grow a business in the EU compared to the USA.

KEY POLICY RECOMMENDATIONS

- 1 Further integrate markets for goods and services, including logistics and network services, and ensure a barrier-free framework that helps wide-scale roll-out of digital technologies.
- 2 Ensure that regulation, at EU and national level, follows the better regulation principles and is properly enforced, with a minimum of administrative burdens in order to support business start-ups and companies' expansion. Competitiveness proofing, including an SME test, must be an integral part of the ex-ante impact assessment for all legislative proposals, and independent scrutiny of impact assessments must be reinforced.
- 3 Energy prices must allow EU businesses to be competitive on international markets. Targeted measures (e.g. reforming taxes and levies, liberalising energy markets, etc.) to address the energy price differential with major competitors and to ensure energy security should be introduced.

4 Trans-European (and national) infrastructure must be significantly improved and expanded. Remaining regulatory, administrative and technical barriers need to be removed to ensure necessary access to infrastructure facilities, inter-connections, inter-operability and to create an investment-conducive regulatory and financial framework.

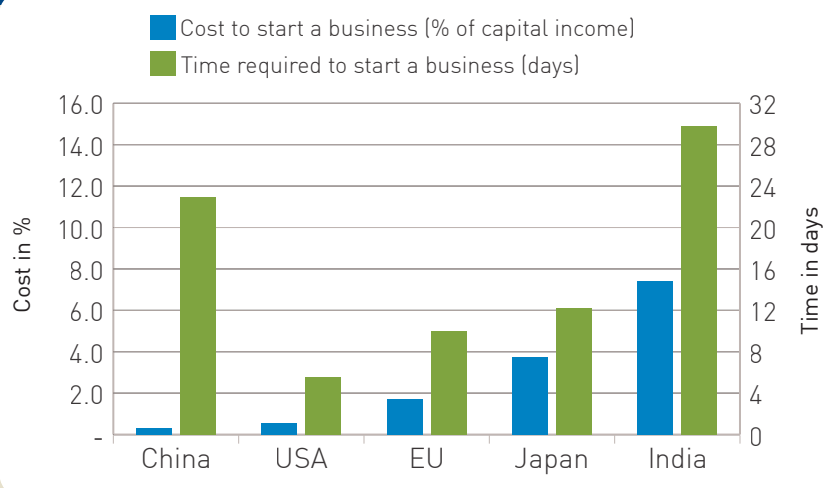
A competitive-friendly business environment is essential for company start-ups and expansion. Open markets with clear and properly enforced rules can promote competition, legal certainty and in turn productivity growth.

The time and cost of starting a business, and of getting operating licences, are key indicators of the overall ease of doing business in an economy. While significant progress has been made over the last decade, administrative hurdles and costs to start up a business continue to vary considerably across the EU, indicating that there is still significant scope to improve. In particular, it continues to cost over three times more to start a business in the EU than in the USA, while the process to start a business in the EU takes almost twice as long as in the USA (graph 7).

Graph 7: Further scope for the EU to reduce administrative burdens

Cost and time to start a business in 2016

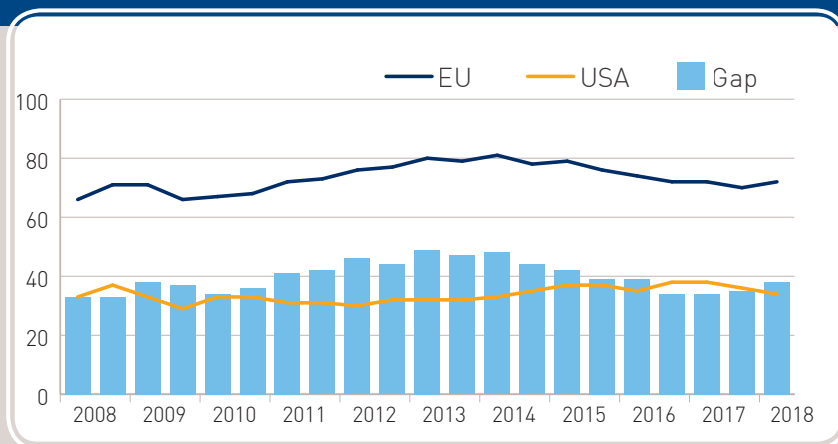
Source: World Bank



It is also extremely complicated to expand and grow on the EU single market. Administrative complexity, regulatory heterogeneity and different approaches in, for example, consumer protection, services or data economy, lead to persistent fragmentation of the single market which does not allow its four freedoms to deliver business efficiencies and productivity gains.

A cornerstone for business success, especially in the manufacturing sector, is the secure supply of competitively priced energy. However, in the EU, retail prices for energy turn out to be significantly higher than in other major economies, in particular the USA. As shown in graph 8, average energy prices for EU industrial producers amounted to €72 per Kwh in the first semester of 2018, which is €38 above the average USA price of €34 or, put in another way, more than twice as high. We can also see that the gap between the USA and the EU has slightly widened in the first half of 2018, which appears to be not related to bilateral exchange rate fluctuations but rather other underlying developments in the energy market.

Graph 8: Industrial energy prices remain about twice as high in the EU than in the USA



Average energy prices for industrial producers in the EU and USA, 1st semester 2008 to 1st semester 2018

Source: BusinessEurope calculations based on Eurostat, EIA and ECB. Methodology from European Commission Energy prices report 2014 & 2016. Does not include confidential rebates over the reference period.

II. INNOVATION AND DIGITAL TRANSFORMATION

KEY OBSERVATIONS

- ▶ EU R&D intensity is much lower in the EU (2.0% in 2016) than in Japan (3.2%) and the USA (2.7%), and is also reflected in the low number of patent applications. China significantly increased its share of spending over the last decade (from 1.4% to 2.1%) and has also overtaken the EU.
- ▶ The EU continues to lag behind its competitors in some key metrics for digital communication. In particular, (fast) fibre connections are much less prevalent in the EU, compared to the leading countries Japan and South Korea.
- ▶ Europe has a strong record in producing robots, particularly for industrial applications, yet this is not matched by our ability to deploy the robots with the EU using fewer robots per employee than our competitors in South Korea, Japan and the USA.

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- 2** More business-oriented innovation policies can ensure a greater economic impact from investment in research and innovation. Targeted initiatives must stimulate private R&D investment and incentives for cooperation between companies, research institutes, and education in networks and clusters of knowledge and competence should be improved in order to facilitate the commercialisation of innovation. Regulation excessively focused on precaution and risk avoidance will stifle investment in innovation.

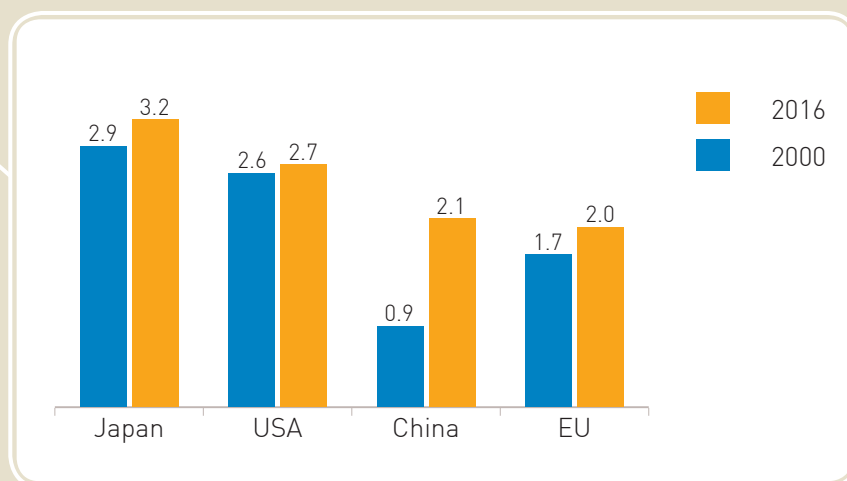
- 3 A strengthened digital infrastructure is essential for the EU to adopt the latest technologies enabling businesses to compete globally. This is especially the case when it comes to providing very high-capacity networks in order to launch 5G on a large scale.
- 4 Ensuring a digital transformation will require a fully functioning integrated digital single market. As well as network investment, action is needed to ensure a barrier-free level playing field for cross-border e-commerce, prevent forced data localisation measures, and to address tried and tested, fit-for-purpose frameworks in the areas of consumer legislation, copyright and data protection rules.
- 5 Europe needs to improve its cybersecurity; it currently invests less in this area than other regions, and as a consequence is slower to respond to threats, increasing uncertainty for business.

The EU's innovation and technological capability is fundamental to our ability to attract and retain high-quality, high-productivity jobs, and take forward the digital transformation that is needed across all sectors to ensure that we are able to compete successfully in the global economy. Measuring innovation capacity and technological readiness is a complex exercise, but R&D investment, (fast) broadband access, patent registrations and estimates to which extent production is automated (e.g. robot density) provide useful pointers in assessing both our current and future capability.

Regarding R&D spending, whilst the EU has slightly increased spending from 1.7% of GDP in 2000 to 2% in 2016, its share remains well below that of the USA (2.7%) and Japan (3.2%). Moreover, the EU was recently overtaken by China (2.1% in 2016), where R&D spending increased rapidly over the last 16 years (graph 9). This also means the EU is a full percentage point behind its own 3% target in the EU growth strategy (Europe 2020).

Graph 9: EU spending on R&D remains well below US and Japanese levels

R&D intensity as % of GDP in 2016



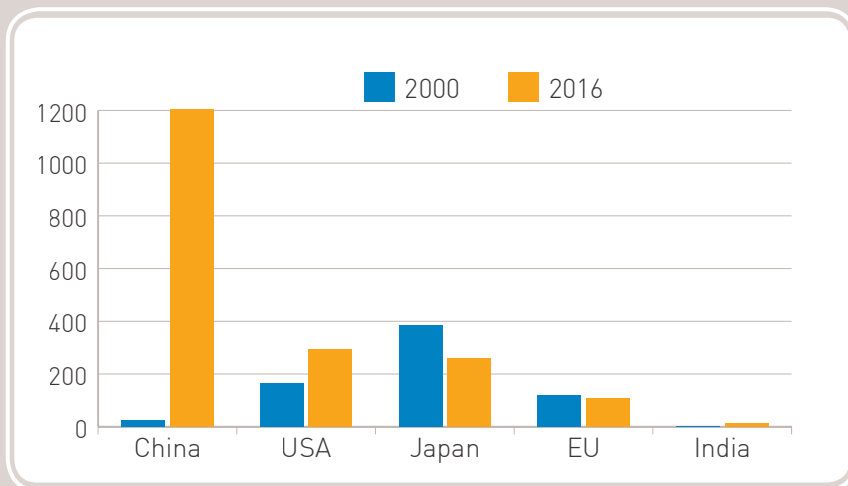
Source: World Bank

Patent applications provide an alternative measure of innovation performance, although companies will use many different methods to protect intellectual property (IP), hence such data should be treated with caution.

As graph 10 illustrates, patent applications stagnated in the EU over the last 16 years, while applications rose steeply in China (from very low levels) and the USA (where applications increased

by almost 80%). As a result, the patent gap between the EU and USA has grown over time, with US application numbers now almost three times above those in the EU (graph 11).

Graph 10: Instead of gradually closing the patent gap, the EU is falling further behind



Total number of patent applications, in thousands

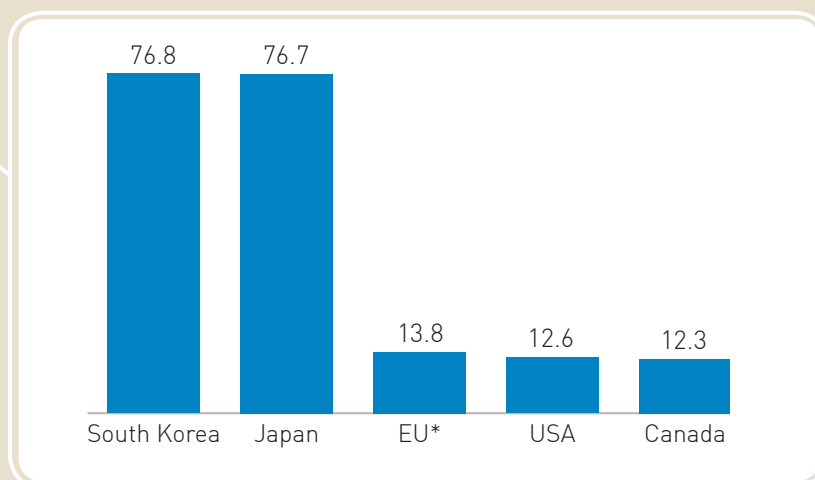
Source: WIPO

Next, broadband as an enabler for economic and social growth has become a key priority of the 21st century.

However, the EU continues to lag behind its competitors in some key metrics for digital communication. As illustrated in graph 11, (fast) fibre connections are much less prevalent in the EU, USA and Canada, compared to the leading countries Japan and South Korea.

Graph 11: The EU, the USA and Canada strongly lag behind the global leaders in fast broadband

Fibre connections in total broadband, in 2017, %

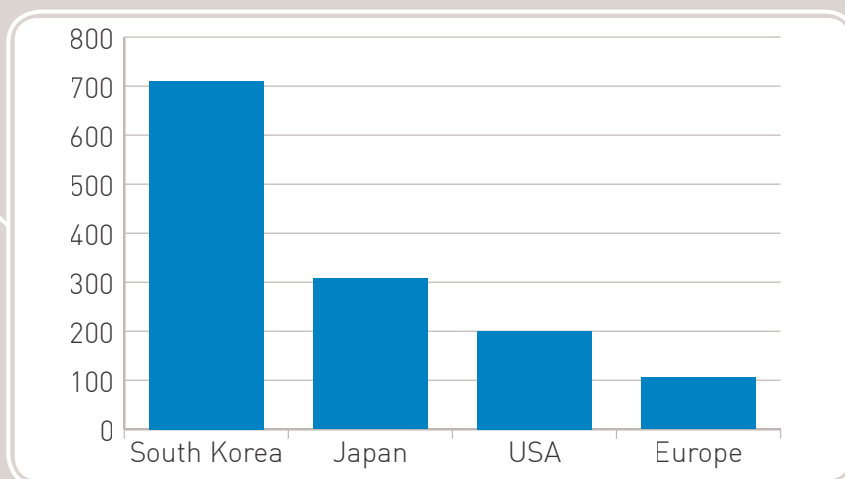


Source: OECD

Finally, the density of installed industrial robots gives a useful benchmark for the capacity of a country to automate production processes. However, while Europe has a strong record in producing robots, particularly for industrial applications, the number of installed robots in Europe, as illustrated in graph 12, is - with only 106 robots per 10,000 employees - significantly below that in South Korea (710), Japan (308) and the USA (200).

Graph 12: Europe's robot density is well below that of other industrialised countries

Number of installed industrial robots per 10,000 employees in the manufacturing industry in 2017



Source: IFR World Robotics 2018

III. LABOUR MARKET & SKILLS

KEY OBSERVATIONS

- ▶ Whilst more than 13 million jobs have been created since the peak of the euro crisis in 2013, the EU unemployment rate (6.7% in November 2018) remains well above that in the US (3.7% in November 2018).
- ▶ Even though unemployment rates are still too high in many member states, businesses increasingly report difficulties in hiring qualified workers.
- ▶ Comparing PISA 2006 and 2015 outcomes suggests that the EU has made little progress in closing the structural difference in education performance with Japan, Canada and South Korea.
- ▶ The average tax wedge is in Europe with 41.5% almost one third higher than in Japan and the USA (both about 32%).

KEY POLICY RECOMMENDATIONS

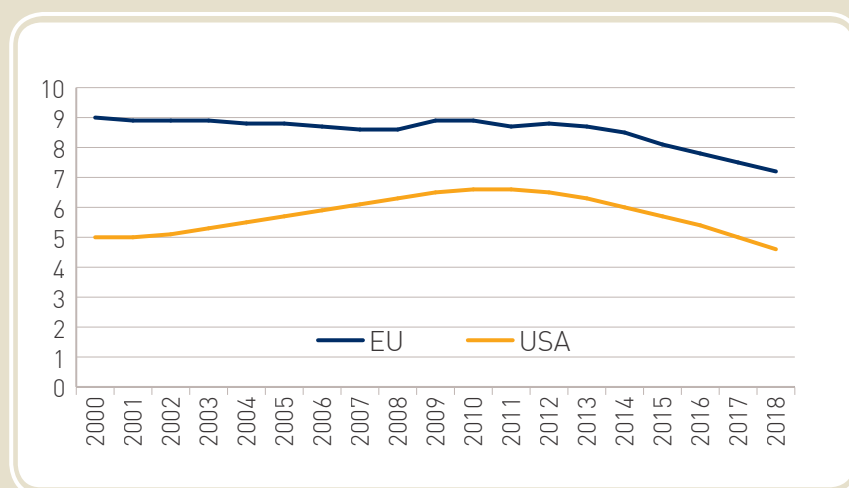
- 1 Urgent policy action is required to avoid labour market mismatches increasingly acting as a break on economic growth. Education and training systems need to be better tailored to labour market needs, particularly with more STEM graduates (science, technology, engineering and maths). An important priority is to achieve well-functioning apprenticeship systems across Europe. This amongst others means progressing towards a majority of the apprentices' training time taking place in the company.

Policy benchlearning and a better use of the European Social Fund is needed to support Member States' reform efforts.

- 2** Improve employment incentives through cuts to tax wedges (non-wage labour costs), particularly for low-income workers, including through lower social security contributions and/or other tax incentives to make work pay, ensuring that taxation does not form a disincentive to work. Open, dynamic and mobile labour markets are needed to support new and more diverse career paths and smooth transitions between jobs, sectors and employment statuses. These more diversified careers need to be accompanied by adequate social security systems promoting professional activity.
- 3** In order to increase global competitiveness, the labour market regulatory framework needs to be clear, simple and flexible. Increases in labour costs must be consistent with rises in productivity growth. This means putting in place policies that can raise long-term productivity.
- 4** Set in motion a genuine partnership for labour market reforms: rather than trying to solve labour market challenges across the board at European level, the European Union's primary role is to provide information, incentives and know-how for member states and social partners to design, implement and evaluate policies addressing the structural labour market challenges they face.
- 5** To mitigate negative impacts of population ageing, reforms must encourage people to stay in the workforce longer, make pension systems sustainable, and integrate legal migrants into the workforce. In order to make social protection systems more effective, social investments should be focussed on areas where they can enhance growth (e.g. skills development, childcare), with the right balance found between adequacy and sustainability of social safety nets.

The EU has seen strong job creation following the peak of the European sovereign debt crisis, with about 13 million jobs created since the beginning of 2013⁴. Alongside strong job creation, the EU saw a gradual fall in unemployment, even though its unemployment rate remains well above that in the USA (6.7% compared to 3.7% in November 2018), with rates in individual member states varying strongly. Whilst estimates of the EU's natural rate of unemployment (the unemployment rate consistent with stable price and wage increases), this remains well above the 4.6% estimate for the USA (graph 13), indicating structural challenges remain on EU labour markets.

Graph 13: The EU's 'natural' rate of unemployment has decreased in the post-crisis period, but at a lower rate than that in the USA



Non-accelerating wage rate of unemployment (NAWRU), in %

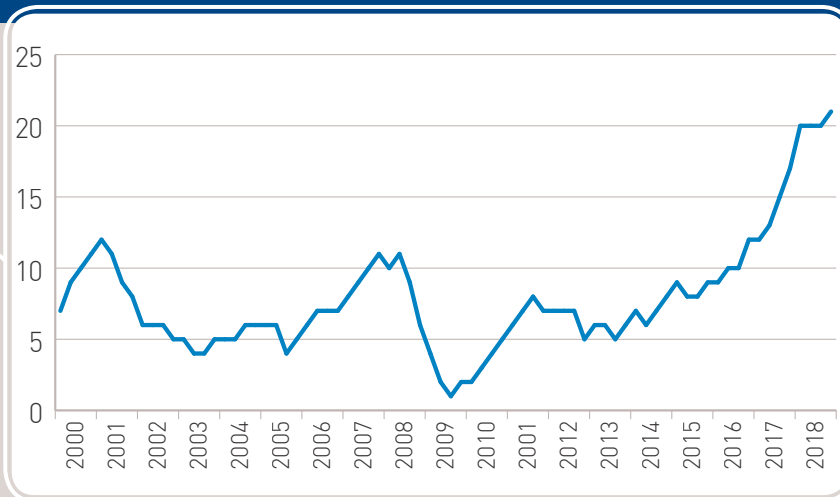
Source: European Commission

⁴ Data between Q1 2013 and Q2 2018 on total employment of 20-64 years old.

A particular concern is that businesses across the EU increasingly report difficulties in hiring qualified workers since the beginning of 2016 (graph 14). Whilst increasing skills shortages might be expected when the economy picks up, the share of industrial enterprises which indicate that insufficient labour limits their production is now twice the pre-crisis share and the highest on record since 1985.

Graph 14: Companies are increasingly concerned that a lack of labour hampers production

Share of industrial enterprises which indicate that insufficient labour limits production, %



Source: European Commission

Against this background, urgent policy action is needed to avoid that labour market mismatches increasingly act as a break on economic growth over the coming years.

Well-functioning labour markets facilitate worker transition between jobs, encourage companies to hire and help match skills supply and demand. In contrast, excessive labour market rigidities make it hard for people to move between jobs, sectors and employment statuses, and may lead to a segmented labour market, reduce a country's attractiveness for both domestic and outside investors, and hamper employment creation as well as productivity and economic growth. It is thus important that labour market frameworks are simple, transparent and predictable, while providing for a variety of employment contracts and ensuring the attractiveness of these different contractual forms.

Many member states are nowadays confronted with the challenge of ensuring clarity at national level on the way in which work opportunities in the context of new business models, such as platform work, qualify in terms of the pre-existing legal definitions of work and self-employment. In some member states, a key priority is to improve the attractiveness of indefinite duration employment contracts. Both at European level and in the member states, more work is needed to increase the coherence between EU and national policies aiming to increase the transparency, portability and/or transferability of social entitlements nationally and cross-border.

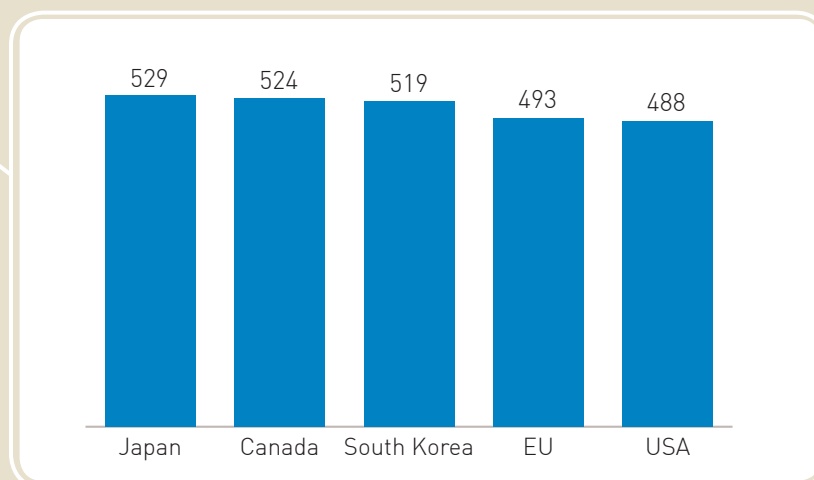
A high quality of education is also key for Europe's competitiveness and addressing mismatches as it ensures that workers have the necessary skills and knowledge throughout their working lives, especially in knowledge-intensive sectors. It is thus of concern that PISA results show that 15-year-old pupils in the EU underperform in comparison to their international peers (graph 15). In 2015, the (weighted) average mean PISA score was 493 in the EU, slightly above that of the USA (488), but well below the scores of pupils in Japan (529), Canada (524) and South Korea (519).

Graph 15: EU pupils underperform in education compared to their international peers

Overall mean score in PISA 2015
(avg. science, reading and mathematics)

Notes: Weighted average score
or the EU.

Source: OECD PISA



The comparably weak performance of EU pupils further underlines the importance of life-long learning. In some systems, school-based learning is widely complemented by other forms such as workplace learning. Examples of this type of “dual system” can be found in Austria, Germany, Denmark, the Netherlands and Switzerland. One advantage of this practice is that it forms a series of public-private partnerships, allowing employers, in particular, and social partners to be involved in the development of vocational and educational training (VET) programmes, particularly apprenticeship schemes, in which they participate in defining and delivering the curricular programmes. Labour market needs and skills shortages can thus be addressed at an early stage.

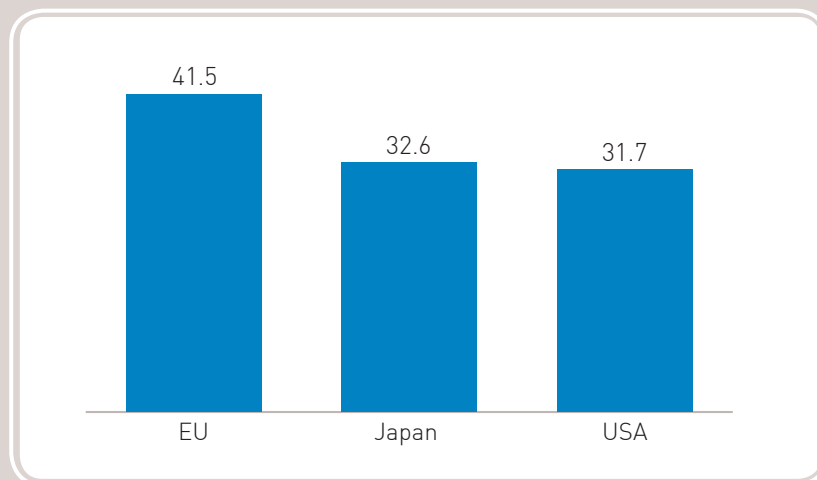
Education institutions should open up more to partnerships with companies, in particular to encourage the development of STEM skills. The quality of initial education needs to be ensured by governments and the right framework conditions should be put in place at national level to encourage governments, companies and workers to invest in life-long learning. The role of the European Union should be to support member states’ efforts to reform their education and training systems so as to better align them with labour market needs. This includes looking at how curricula can be adapted over a shorter time period.

Next to targeted initiatives to improve education and training systems, labour mobility can also help in alleviating mismatches. On top of that, labour mobility is particularly important in a monetary union to ensure that different economies react optimally to a common monetary policy, as it can serve as an adjustment mechanism in response to asymmetric shocks. However, in the EU only around 0.3% of the population is moving from one country to another each year, comparing unfavourably with the USA where 3% of the population moves to another state each year⁵.

In addition, the high tax burden across Europe has to be addressed. Both the OECD and the European Commission stress that high levels of labour taxation may have detrimental effects on employment by reducing incentives both for workers to enter the labour market (if net gains after taxes and benefits are small) and employers to hire more staff (if labour costs are very high). Thus, it is a clear concern that the average tax wedge is in the EU about 30% higher than in the USA and Japan (graph 16), with no effective progress made in the EU over the last decade.

⁵ CEPS, “Labour Mobility in the EU’s Addressing challenges and ensuring ‘fair mobility’”, July 2016.

Graph 16: The tax wedge on labour in the EU needs to come down



Tax wedge on average-income earners (single person) in 2017

Source: OECD

IV. ACCESS TO FINANCE AND FINANCIAL STABILITY

KEY OBSERVATIONS

- ▶ While the Euro-area as a whole has made progress in reducing non-performing loans (NPLs) since 2012, NPLs were 3.4% of GDP in 2017, still well above the 1.1%-1.2% seen in the USA and Japan.
- ▶ Euro-area businesses fund themselves to a larger extent via bank lending compared to the USA, where companies rely more on capital markets. Stock market capitalisation (as % of GDP) in the Euro-area is less than half that in the USA.
- ▶ The gap in terms of venture capital funding with the USA has increased in recent years. \$19 bn were invested in the EU in 2018, compared to \$86 bn in the USA.
- ▶ Whilst Euro-area banks now feel more confident in lending again outside the EU, their lending to other banks, institutions and firms within the Euro-area, but outside of their own member state has fallen strongly in recent years, despite the first steps being put in place to complete the banking union.

KEY POLICY RECOMMENDATIONS

- 1** Particularly in light of the UK leaving the EU, reinforce and implement the Capital Markets Union to ensure that the EU puts in place a genuine single market in financial services, and develops complementary sources of finance to bank lending.
- 2** Take action to ensure prudential rules strike the right balance between increasing financial stability and supporting companies' financing needs for investment and business activities.

- 3 A full banking union must be put in place, with rapid agreement and implementation of an EU deposit insurance scheme, alongside the existing supervision and resolution pillars, needed to address the continued fragmentation of EU savings and credit markets. However, further asset quality reviews of all banks are necessary before establishing a common system.
- 4 Address still high levels of NPLs in many European banks in a way which increases new lending and maintains financial stability.

Access to finance on reasonable terms is a pre-condition for companies to thrive and make the investment necessary to drive growth and maintain competitiveness. In order to both provide stability and meet the different financing needs of companies, and of SMEs in particular, finance needs to be available through a variety of different channels.

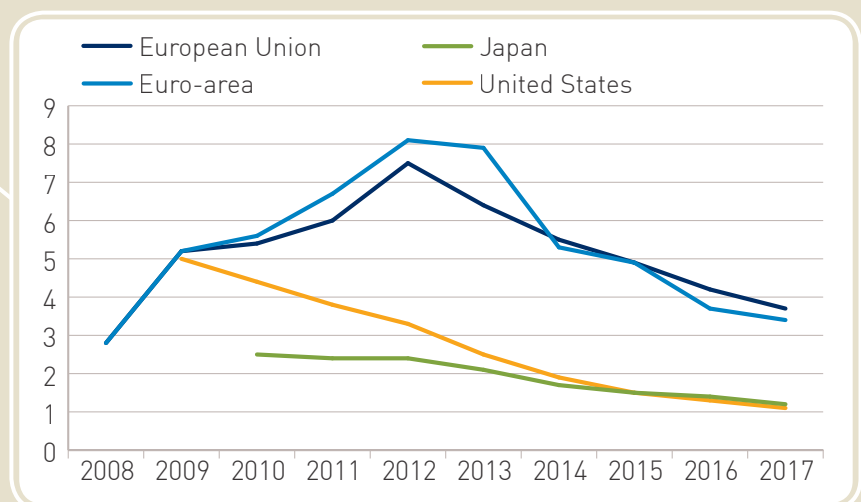
Financial instability, as illustrated during the crisis, impacts negatively on access to finance, confidence and growth, precluding companies from taking on new investment. The negative feedback loop between sovereign and bank financial positions we saw building up from 2010, which led to political uncertainty and financial market instability, has become less acute since 2012, following strong European Central Bank (ECB) action and the banking union. However, both the legacies of the financial crisis and the increasingly stringent prudential regulation of banks continue to impact upon bank lending to businesses, especially to SMEs, and in those countries that were hit the hardest by the crisis.

One particular supply constraint on bank lending in the Euro-area may be the continuing high volumes of non-performing loans (NPLs) that banks continue to hold on their balance sheets in a number of member states. While the Euro-area as a whole has made progress in reducing NPLs since the heights in 2012, when the ratio of NPLs to gross loans amounted to over 8%, NPLs were with 3.4% in 2017 still well above the 1.1-1.2% seen in the USA and Japan (graph 17). In addition, the ratio of NPLs varies significantly across Euro-area member states, ranging from 0.7 to 45.6%. The ECB has estimated that if the capital tied up to support NPLs could be deployed to support new lending then 'total credit volume' in the Euro-area could increase by at least 2.5% overall, and at least 6% in the six member states with the highest concentration of NPLs⁶.

Graph 17: While NPLs have gradually been reduced across Europe, ratios still remain above those in the USA and Japan

Bank non-performing loans to total gross loans (%)

Source: World Bank Group

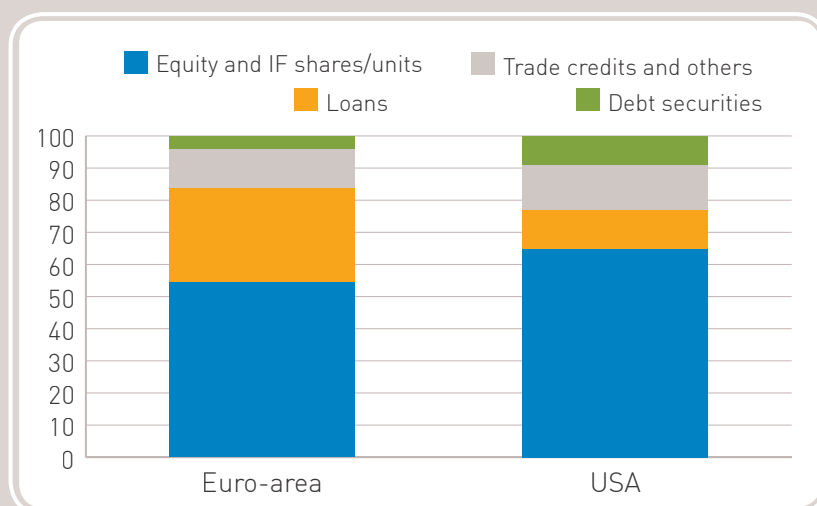


⁶ Keynote speech by Vítor Constâncio, "Resolving Europe's NPL burden: challenges and benefits" (February, 2017)

A key project for the period ahead will be to reinforce and implement the Capital Markets Union, particularly in light of the UK's withdrawal from the EU, to ensure that the EU establishes a genuine single market in financial services and develops complementary sources of finance to bank lending.

Euro-area businesses fund themselves to a much larger extent via bank lending as shown in graph 18, with loans making up over 29% of total liabilities of non-financial firms, in contrast to only 12% in the USA where firms fund themselves to a greater extent via capital markets. First, equity and investment fund shares/units make up 65% of firm liabilities in the USA, but only 54% in the EU. Second, debt securities such as bonds amount to 10% in the USA, but only 4% in the Euro-area. Moreover, the structure of liabilities of non-financial firms since the financial crisis is largely unchanged despite several EU policy initiatives to diversify firm funding sources following the crisis.

Graph 18: Euro-area businesses fund themselves to a larger extent via bank lending compared to the USA, where companies rely more on capital markets



Main liabilities of non-financial firms as % of total liabilities in 2017

Source: OECD

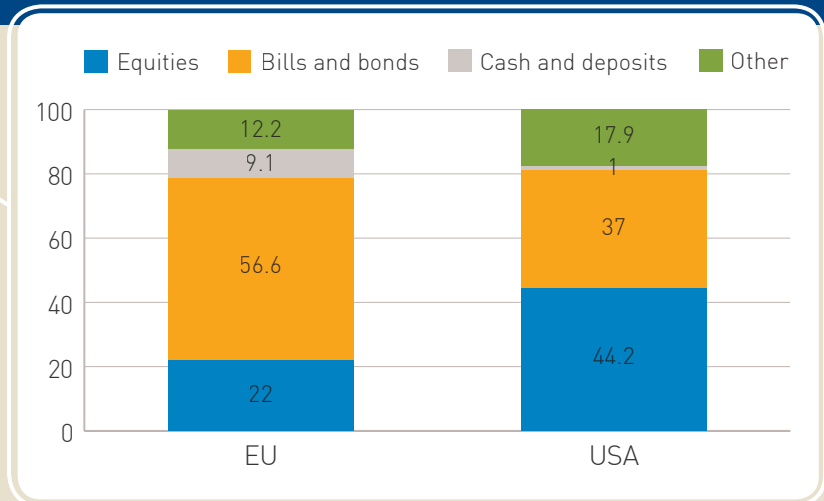
If we were to look at absolute values, the differences in size of market-based financing between the Euro-area and USA are even more pronounced when it comes to listed equities, given that in Europe a large share of equity is unlisted. This is reflected in stock capitalisation which is with 78% of GDP in the Euro-area well below that in the USA (166% of GDP). Moreover, stock capitalisation fell slightly in the Euro-area since the financial crisis (-2 pp), while it increased by 28 pp in the USA.

Similarly, there are also striking differences in the allocation of pension fund assets in the EU and USA. As shown in graph 19, the share of equities as asset class in EU pension funding is only half that in the USA. In contrast, the EU relies to a much greater extent on bills and bonds (57% compared to 37% in the USA).

Graph 19: The share of equities as asset class in EU pension funding is only half that in the USA

Pension fund asset allocation for the EU and USA, 2015 (% of total investment)

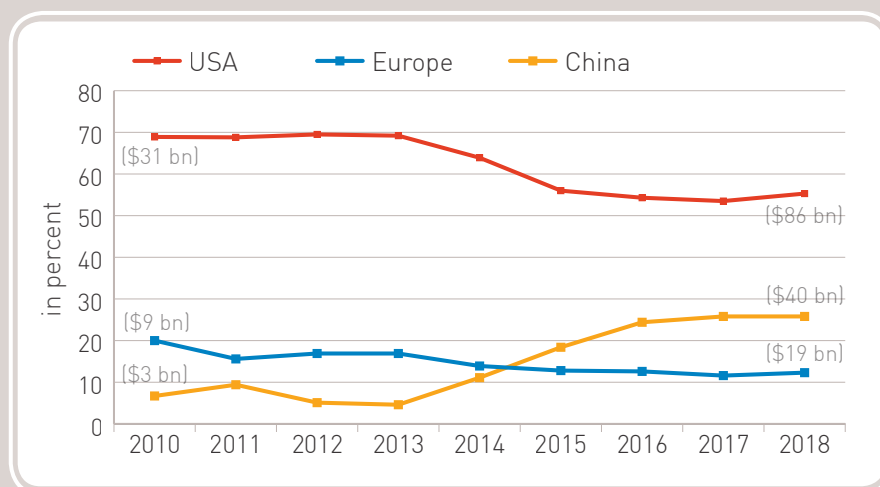
Source: AFME based on OECD data



Expanding the financial support channels can help companies to avoid credit shortfalls and obtain better credit conditions, while at the same time contributing to financial stability by diversifying the risk between banks and other financial institutions.

Venture capital (VC) can also be an important source of finance, in particular for growth companies. In terms of global shares, we have seen a strong increase in China since 2010, which implied that the respective shares of the EU and USA have fallen (graph 20). While we saw a doubling of VC investment in the EU in absolute terms since 2010, investment in the USA increased by almost 2.8 times, implying the gap between the EU and USA increased even further (2018: \$19 bn invested in the EU vs. \$86 bn in the USA). In particular, the EU lacks the large VC funds found in the USA, with the period of investment also being shorter in the EU.

Graph 20: EU strongly lags behind the USA for venture capital financing and was recently overtaken by China



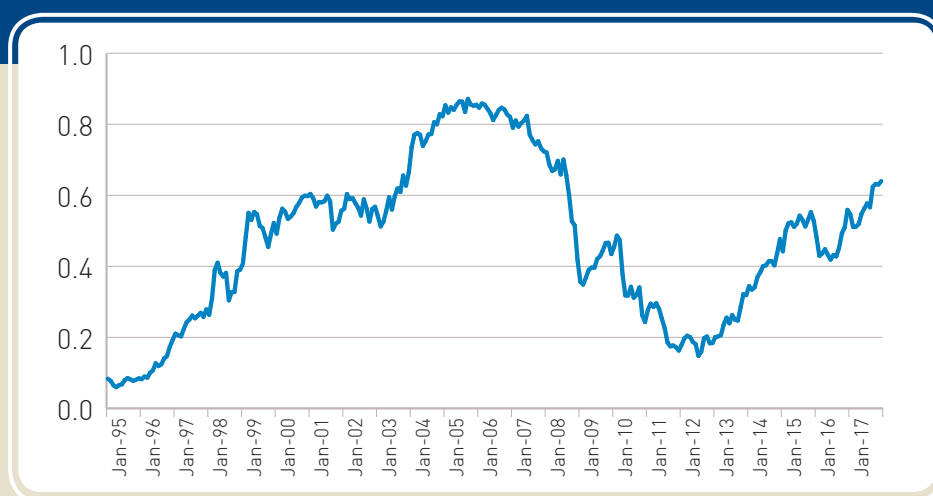
Venture capital invested in Europe, the USA and China as a share of global total. Absolute amounts in brackets for 2010 and 2018

Source: KPMG, Venture Capital Pulse

Deepening the Economic and Monetary Union and in particular completing the banking union continues to be a key challenge for European policy-makers in the coming years. EU leaders will need to make firm decisions to strengthen our common currency. In particular, a full banking union must be put in place, with rapid agreement and implementation of an EU deposit insurance scheme, alongside the existing supervision and resolution pillars, which are needed to address the continued fragmentation of EU savings and credit markets.

As shown by the ECB composite indicator of financial integration (graph 21), Euro-area financial markets fragmented in the aftermath of the financial crisis, and while the indicator points to a reintegration trend since 2012, financial markets are still more fragmented compared to what they were in the pre-crisis period in 2005-2007.

Graph 21: Financial integration has not returned to pre-crisis levels



Price-based composite indicator of financial integration in the Euro-area

Source: European Central Bank

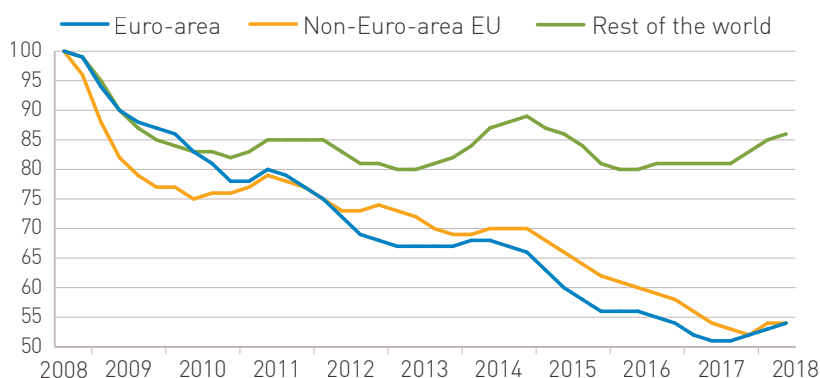
Notes: The composite indicator aggregates ten sub-indicators covering the period from January 1995 to December 2017. It lies between zero (full fragmentation) and one (full integration).

Similarly, graph 22 illustrates this fragmentation by showing the claims held by Euro-area banks in different countries. As is well known, following the financial crisis, banks across the globe reduced their international lending, and Euro-area banks were no exception to this. But whilst Euro-area banks soon felt more confident in lending again outside the EU, their lending to other banks, institutions and firms within the Euro-area, but outside of their own member state, has fallen strongly in recent years, despite the first steps being put in place to complete the banking union. Only since 2017 has there been a slight increase in lending to counterparts in the EU/Euro-area, but it remains to be seen if this is a permanent trend or just a temporary incidence. As the ECB has pointed out, greater cross-border banking can increase financial stability and competition in the banking sector, ultimately improving the availability of finance for firms to invest – meaning completing the banking union really is a key priority.

Graph 22: Intra-Euro-area bank lending continues to fall despite banking union

Cross-border bank claims of Euro-area banks by destination country, Q3 2008 – Q2 2018

Source: BusinessEurope calculations from Bank of International Settlements data



V. TAXATION AND PUBLIC FINANCES

KEY OBSERVATIONS

- ▶ Much more remains to be done to reduce EU public debt levels which at 81% of GDP are still well above the 60% Maastricht limit.
- ▶ Public expenditure in the EU is 45% of GDP, well above levels in Japan (37%) and the USA (36%).
- ▶ The share of growth-friendly public spending in overall spending is just 30.9% in the EU, compared to 44.9% in the USA.

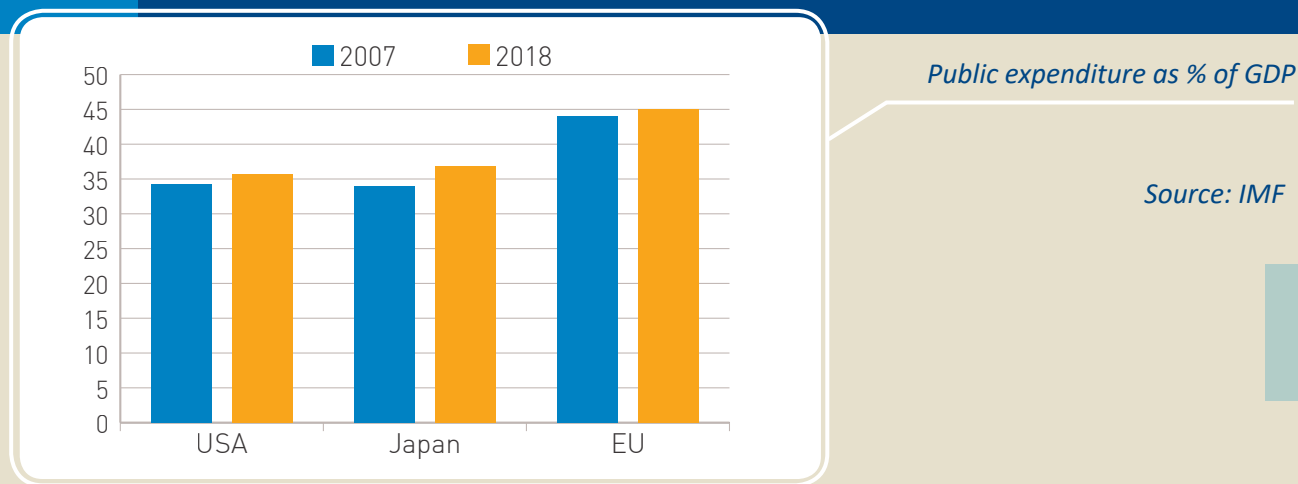
KEY POLICY RECOMMENDATIONS

- 1** In all member states, there is scope for making public finances growth-friendlier and more efficient, in particular by targeted reductions in non-productive public spending and by reductions in distortionary taxes that hamper growth.
- 2** Proper implementation of the Stability and Growth Pact (SGP), drawing on built-in flexibility, remains essential to help member states put their public finances on a sustainable footing. This is key in order to strengthen investors' trust in the Euro-area. But it is also essential that the SGP gives the fullest support possible to member states who wish to orientate their budgets towards investment and growth-supporting expenditure.
- 3** Tax reforms should reduce taxation on labour and capital, including corporation tax, which are particularly damaging to growth and employment.
- 4** Member states should continue their efforts to ensure the administration of their tax systems becomes simpler, more transparent and user-friendly.

Sustainable public finances are of key importance for long-term growth. The financial crisis illustrated that falling confidence in a government's ability to repay debt can lead to a vicious circle whereby increased borrowing levels lead to higher borrowing costs, and in turn require higher taxation.

Public expenditure remains with 45% of GDP in the EU well above the 37% in Japan and 36% in the USA (graph 23).

Graph 23: EU public expenditure ratios are well above those seen in other economies



To some extent, the bigger role of the state in Europe relates to policy choices made at national level to ensure sustainability and adequacy of social protection systems, including the provision of public healthcare, pensions and welfare systems. Nevertheless, public expenditure needs to be financed by taxes which, if too high, can be harmful for growth by weakening incentives for both investment and workers to enter the labour market. Progress towards fiscal sustainability therefore needs to ensure greater efficiency of the public sector and quality of public finances, with special attention to growth-enhancing investment, while avoiding tax increases.

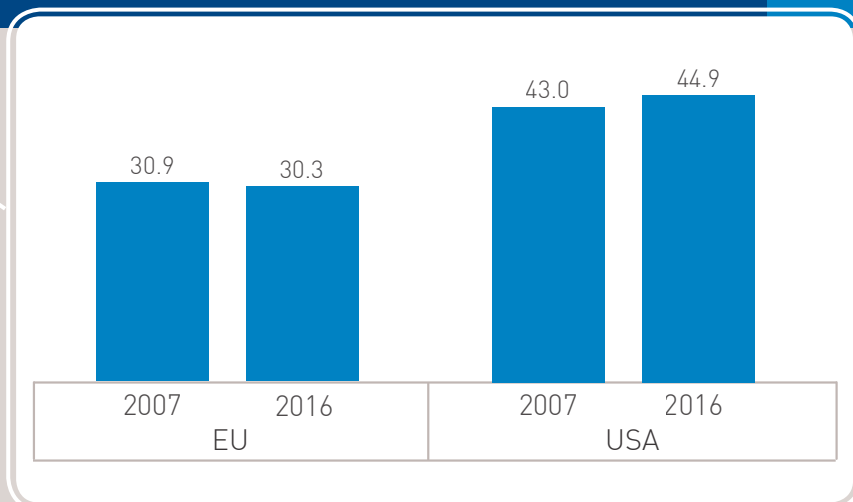
Against this background, it is a concern that growth-friendly public spending as a share of total public spending decreased slightly in the EU over the least ten years (from 30.9% in 2007 to 30.3% in 2016), increasing the gap between the EU and the USA even further, where the share of growth-friendly spending increased (from 43% in 2007 to about 45% in 2016) (graph 24). All EU member states should therefore review the composition of their public expenditure to make it more supportive of growth.

Graph 24: The USA spends a much higher share on growth friendly items than the EU

Share of growth-friendly public spending in overall spending in 2007 and 2016, in %

Note: Expenditure assumed to be growth-enhancing: education, R&D, health, transport and communications

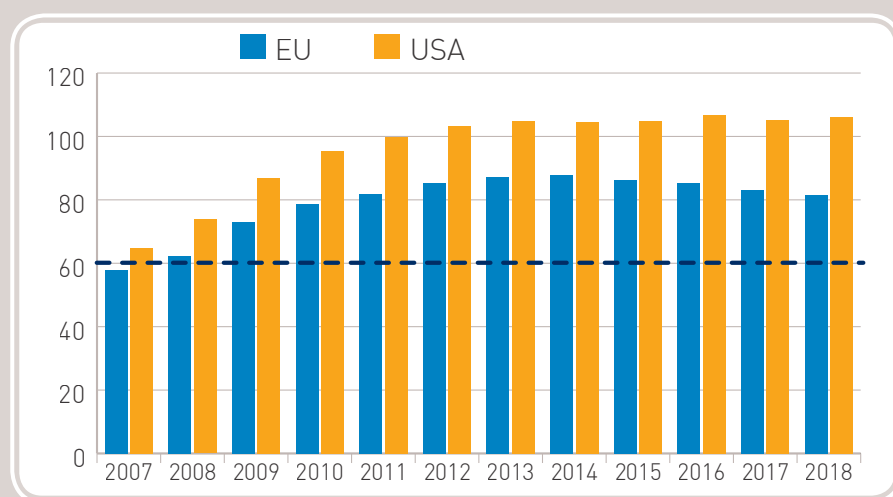
Source: Eurostat, OECD COFOG database and Bureau of Economic Analysis



Finally, while it is positive to observe that EU member states have made significant progress in reducing public deficit since the financial crisis (from -6.6% of GDP in the EU in 2009 to -0.7% in 2018)⁷, there remains more to be done to reduce still high public debt ratios. Even though public debt as a share of GDP is below that of the USA (81% vs. 106%), it remains well above the 58% in 2007 and the 60% Maastricht limit (graph 25).

In this context, proper enforcement of the Stability and Growth Pact (SGP) remains essential to help member states put their public finances on a stronger footing, and in particular bring down debt levels below the Maastricht threshold. However, it is also essential that the SGP offers the fullest support possible to member states who wish to orientate their budgets towards investment and growth-supporting expenditure.


Graph 25: The EU public debt ratio is below that of the USA, but still well above the 60% limit set out in the Stability and Growth Pact



Gross public debt as % of GDP

Source: IMF

⁷ In the Euro-area, the public deficit fell from -6.2% of GDP to -0.6% during the same period.



PART 2: STRUCTURAL REFORM PROGRESS - MEMBER FEDERATIONS' ASSESSMENT

As Part 1 of this report demonstrates, a failure to take structural reforms forward has had a significant impact on Europe's competitiveness and in turn on its economic performance. The potential benefits from reform are huge with the OECD⁸ suggesting for example that "if countries were to move to best practice in product and labour market policy settings, aggregate output in the Euro-area could rise by more than 6% by 2025". Such an improvement would almost halve the per capita gap with the USA by 2030. Reforms can also be important in increasing the resilience of the EU economy, with for example, ECB research suggesting that "sound labour and product markets, framework conditions and political institutions" could **reduce the probability of a severe recession by around 20%**⁹.

Against that background, this chapter analyses the results of a survey of BusinessEurope member federations regarding reform effort over the year 2018, linked to the European Semester. In particular, federations commented on the appropriateness of each of the Commission's country-specific recommendations (CSRs) and on their government's efforts to implement them. Detailed answers by member federations on individual country recommendations can be found on BusinessEurope's website.

I. COUNTRY-SPECIFIC RECOMMENDATIONS

The survey of our member federations shows that the EU's CSRs continue to be in line with businesses own reform priorities. BusinessEurope member federations believe that **90% of the CSRs** (a slight increase compared to 89% last year) address issues that are either important or extremely important, with nearly all of the remaining 10% of CSRs seen as helpful.

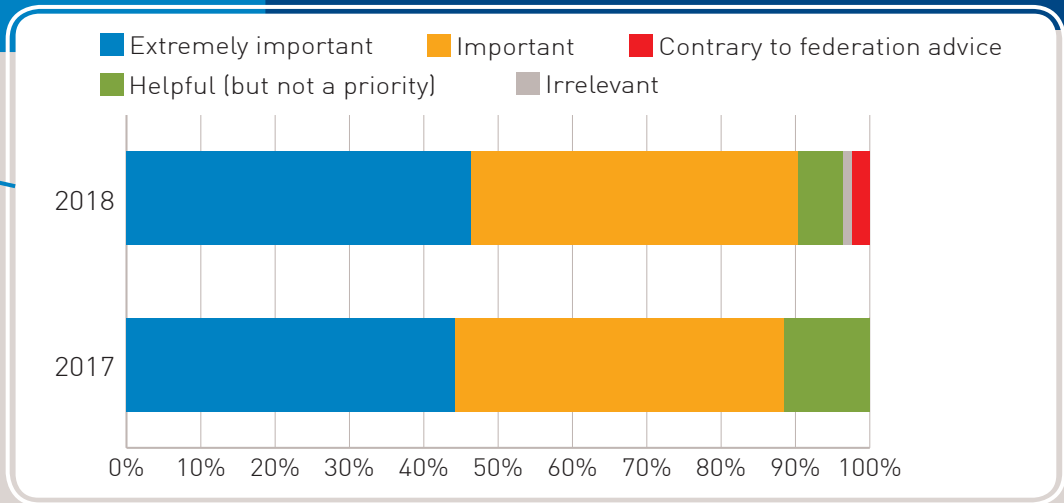
⁸ OECD, "Economic Challenges and Policy Recommendations for the Euro Area". Better Policies Series, 2014.

⁹ "ECD - Working Paper - Sondermann, D. (2016), "Towards more resilient economies: the role of well-functioning economic structures", Working Paper Series, No 1984, ECB, Frankfurt am Main, November.



Assessment of the 2018 country-specific recommendation objectives

Member federations' assessment of the appropriateness of individual CSRs



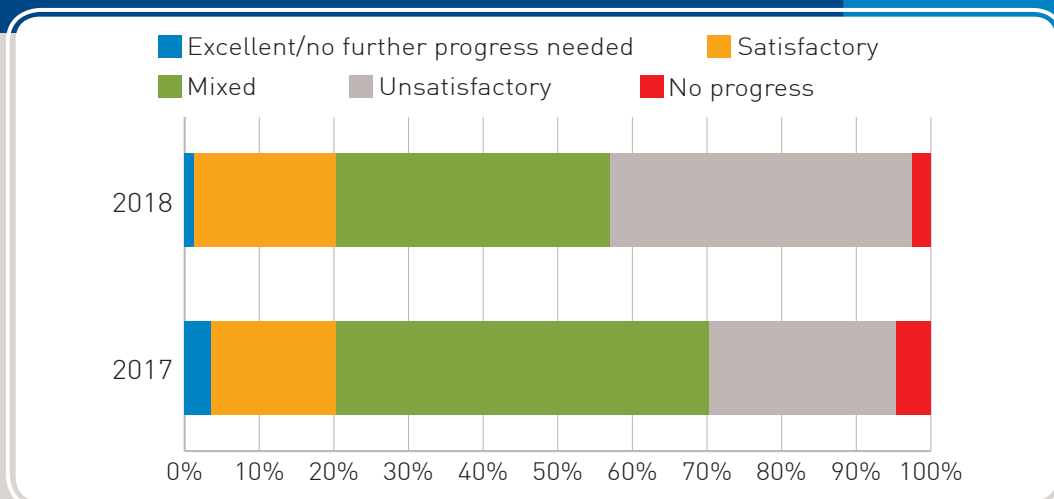
Source: BusinessEurope survey of member federations

However, despite the importance of these recommendations, our member federations conclude that **only 20% of the 2018 CSRs assessed are satisfactorily implemented**. While the figure increases to 57% when considering the CSRs where mixed (i.e. some) progress has been identified, this still means that over 40% of CSRs have been seen as unsatisfactory or no progress at all.

As in previous years, reforms continue at different paces in different member states. There are examples of countries making positive reform progress, in particular in Estonia, Hungary and Portugal where the pace of reform implementation has picked up compared to last year. However, in some countries, reform implementation has fallen, notably in Belgium, Spain and Italy.

Progress in implementing the 2018 country-specific recommendations

Member federations' assessment of member states' efforts to implement recommendations



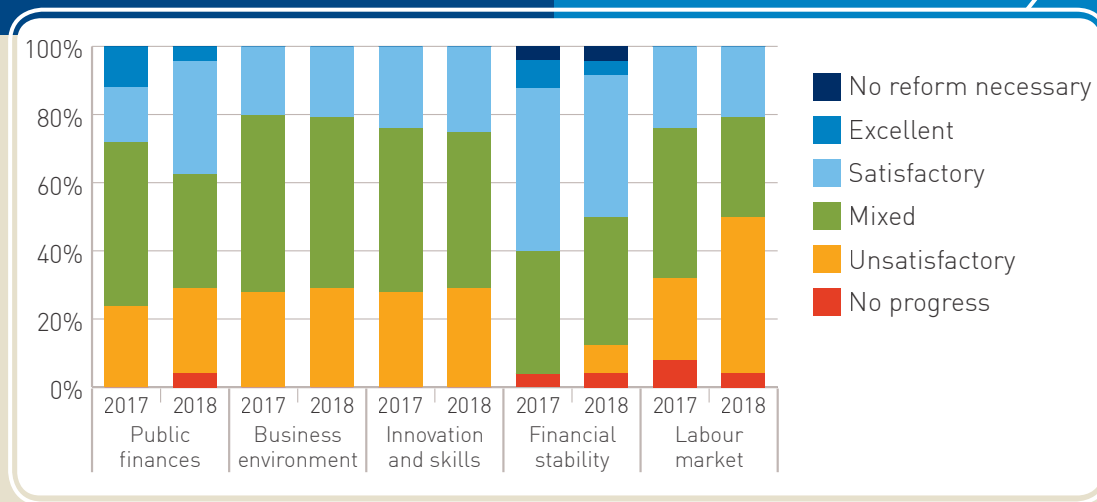
Source: BusinessEurope survey of member federations

II. PROGRESS BY AREA

In addition to assessing reform effort in implementing the country-specific recommendations, BusinessEurope member federations have assessed reform progress in five broad policy areas that are important for long-term growth and which also correspond to the areas analysed in part 1 of this report.

Reform progress by main policy areas

Member federations' assessment of reform progress by main areas



Source: BusinessEurope survey of member federations

- The most pressing concern remains the slow pace of reform on the labour market according to our members, an area highlighted as the priority for reform in last year's Reform Barometer amidst signs of rapidly increasing skills shortages. Nearly 50% of federations now consider reform progress in this area to be (at best) unsatisfactory (compared to around 30% in 2018).
- However, across all broad policy areas, an increasing proportion of federations consider reform progress to be unsatisfactory or worse, further emphasising the slowdown in reform efforts.

III. REFORM PRIORITIES FOR 2019

We have also surveyed our member federations regarding future reform priorities, with the results summarised in the following chart:

Reform priorities for 2019

Member federations' assessment of priorities for reform in 2019

Source: BusinessEurope survey of member federations

	Difference from 2018
1. Labour market mismatches and labour mobility	=
2. Tax reforms	+1
3. Business environment	+1
4. Pension and healthcare reforms	-2
5. R&D and innovation	+1
6. Public sector efficiency	-2
7. Public investment	+1
8. Wage bargaining and wage-setting policies	+7
9. Labour supply measures	=
10. Making work pay: interplay of tax and benefit system	+1

Our members have once more highlighted the need for reform on the labour market as a key priority for 2019, following - as noted above - worrying signs of a loss of reform momentum in this area. In particular, measures to improve labour market mobility can help ensure that workers are able to maximise the use of their training and specialist skills in their jobs. Furthermore, members are increasingly concerned about the slow pace of reform in wage-bargaining and wage-setting policies.



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