

## **20090703 Background on ECOFIN meeting Tuesday 7 July**

### **Source: Council**

The Council will be preceded by a meeting of the eurogroup, on Monday 6 July starting at 17.00.

Ministers will hold a breakfast meeting on Tuesday at 9.00 to discuss the economic situation and developments on financial markets, on the basis of an update by the Commission and the European Central Bank. They will also take note of progress on the Marguerite Fund, a European equity fund for energy, climate change and infrastructure to be launched by the European Investment Bank and other financial institutions, as well as on the EU's investment framework for the Western Balkans.

Starting at 9.45, the Council is due to open excessive deficit procedures for Latvia, Lithuania, Malta, Poland and Romania, issuing recommendations on corrective measures to be taken. It will adopt a new recommendation on measures to be taken by Hungary to correct its excessive deficit, and will review a number of member states' stability and convergence programmes.

The Council is also due to adopt conclusions on pro-cyclicality, which is the term given to the perceived exacerbation of fluctuations on volatile financial markets. It will examine ways of reducing the pro-cyclical effects of financial regulation, as regards bank capital requirements and accounting standards, for instance. Amongst the other items on its agenda, the Council will discuss preparations for G-20 meetings planned for September: G-20 finance ministers' meeting and G-20 summit.

Ministers will then join their Mediterranean counterparts for a Union for the Mediterranean ministerial meeting (UfM). The meeting will continue over lunch, during which the Euro-Mediterranean Investment and Partnership Facility (FEMIP) will be discussed.

### **Presidency work programme**

- Public deliberation

The Swedish presidency will present a work programme for economic and financial affairs for the duration of its term in office (July to December 2009), and the Council will hold a public deliberation ([doc. 11444/09](#)).

Since last autumn, the European economy has faced unprecedented challenges. Turbulence in capital and credit markets, coupled with reduced global demand and a high degree of uncertainty, has resulted in the most severe downturn since the 1930s.

The EU and the member states have acted jointly to manage the crisis. A wide range of measures have been taken to restore confidence in financial markets, and the European Council has agreed on an economic recovery plan that has softened the impact of the crisis on growth and employment.

The Swedish presidency will oversee implementation of these measures and will further promote measures to facilitate a rapid yet sustainable recovery.

As regards the work of the Economic and Financial affairs Council, the presidency programme establishes the following priorities:

- o improving supervision and regulation of financial markets;
- o re-establishing sound public finances;
- o tackling labour market challenges;
- o reinvigorating the EU's Lisbon strategy for growth and jobs post 2012;
- o advancing international climate negotiations.

### **Follow-up to the European Council**

The presidency will inform the Council of the follow-up to be given to the European Council meeting on 18 and 19 June, in particular as regards the supervision of financial services.

## **Preparation for G-20 meetings**

The presidency will outline the approach it intends to follow in the preparation of G-20 meetings scheduled for September and the Council will hold an exchange of views.

A meeting of G-20 finance ministers and central bank governors is planned for 3 and 4 September in order to prepare a G-20 leaders meeting to be held in Pittsburgh (United States) on 24 and 25 September as part of an ongoing process aimed at restoring economic confidence and financial stability worldwide.

The Pittsburgh summit will bring together the heads of state and government of the world's developed and emerging economies, as well as representatives of international financial institutions. It will follow on from summits held in Washington on 15 November 2008, the first G-20 meeting to be held at the highest level, and in London on 2 April 2009.

## **Pro-cyclicality and the regulation of financial services**

The Council will hold an exchange of views on means to reduce pro-cyclicality on financial markets, in the light of a report from the Economic and Financial Committee ([11479/09](#)), and is due to adopt conclusions ([doc. 11478/09](#)).

Pro-cyclicality is the term given to the perceived exacerbation of fluctuations on volatile markets. The discussion is likely to focus on the possible pro-cyclical effects of regulation, in particular bank capital requirements and accounting standards.

In November 2008, G-20 leaders called on international bodies to address pro-cyclicality, by mitigating it in regulatory policy and reviewing how the valuation and leverage of assets, bank capital requirements, compensation schemes and provisioning practices may exacerbate cyclical trends.

At its meeting on 18 and 19 June, the European Council called on the Commission and the member states to accelerate work on countering the pro-cyclical effects of regulatory standards, as regards bank capital requirements and impaired assets for instance. It also invited the member states to take action rapidly on executives' pay and on remunerations in the financial sector, taking account of recommendations made by the Commission.

Both regulatory standards and executive pay are covered by the EFC report, which identifies four main policy responses:

- o the monitoring of system-wide risks;
- o the building of counter-cyclical buffers through capital and provisions;
- o the improvement of accounting rules; and
- o the establishment of a sound framework for remuneration schemes.

Beyond measures aimed at reducing the pro-cyclical effects of financial regulation in the future, the draft conclusions highlight the need to continue developing short-term measures to overcome the current economic crisis.

## **Excessive deficit procedures - Latvia, Lithuania, Hungary, Malta, Poland and Romania**

The Council is due to adopt, under article 104(6) of the treaty, decisions on the existence of excessive government deficits in Latvia, Lithuania, Malta, Poland and Romania, and recommendations, under article 104(7), on corrective action to be taken.

It is also expected to adopt a revised recommendation, under article 104(7) of the treaty, on measures to be taken by Hungary in order to correct its excessive deficit.

The treaty sets a 3% reference value for the ratio of planned or actual government deficit to gross domestic product (GDP). In Latvia, Lithuania, Malta, Poland and Romania, that threshold has been exceeded and an excessive deficit procedure will be opened. In the case of Hungary, a procedure is already open and the recommended timetable for correction of the deficit will be revised.

In its recommendations, the Council is due to set 7 January 2010 as a deadline for all six member states to take corrective action.

On the basis of the outlook provided by the Commission in its spring 2009 economic forecasts, the Council is expected to call on Latvia to reduce its deficit below the 3% of GDP threshold by 2012, Lithuania to do so by 2011, Malta by 2010, Hungary by 2011, Poland by 2012 and Romania by 2011.

The Council is expected to find that special circumstances in Latvia, Lithuania, Poland and Romania allow for correction of the deficit in the medium term. In the case of Malta however, it will consider no departure from the standard deadline for correcting the deficit to be warranted. As regards Hungary, it is expected to find that a revised timetable for correction of its deficit is justified.

Adoption of the article 104(6) decisions requires a qualified majority in the Council; adoption of the article 104(7) recommendation requires a majority of two-thirds of the weighted votes of 26 delegations (excluding the delegation concerned).

#### Latvia

Latvia has requested assistance from international lenders, obtaining a EUR 3.1 billion loan from the EU in January as part of a EUR 7.5 billion package of assistance. According to figures notified by the Latvian authorities, the general government deficit reached 4% of GDP in 2008, thus exceeding the 3% reference value, and is expected to widen in 2009.

The Commission's recommendation for a Council recommendation calls on Latvia to ensure an annual average fiscal effort of at least 2.75% of GDP over the 2010-12 period, in order to bring the deficit back below 3% of GDP in 2012.

#### Lithuania

In the case of Lithuania, the Council is expected to consider special circumstances to exist on account of the size of the required adjustment and the very weak economic outlook. According to figures notified by the Lithuanian authorities, the general government deficit reached 3.2% of GDP in 2008, thus exceeding the 3% reference value. And the deficit is expected to widen in 2009 and 2010, despite the government's consolidation efforts.

In its recommendation, the Council is expected to call on Lithuania to ensure an annual average fiscal effort of at least 1.5% of GDP over the 2009-11 period, in order to bring the deficit back below 3% of GDP in 2011.

#### Malta

According to figures notified by the Maltese authorities and validated by Eurostat, Malta's general government deficit reached 4.7% of GDP in 2008. The breach of the 3% of GDP reference value was more due to developments in expenditure than the impact of the economic downturn.

In its recommendation, the Council is expected to call on Malta to ensure that budgetary measures planned for 2009 are rigorously implemented, whilst avoiding any further deterioration in public finances, and to spell out new consolidation measures in order to bring the deficit back below 3% of GDP in 2010.

#### Hungary

Hungary has been subject to an excessive deficit procedure since July 2004, when the Council also issued a recommendation under article 104(7) of the treaty. The Council issued further article 104(7) recommendations in March 2005 and October 2006, having found in January 2005 and November 2005, by decisions under article 104(8), that effective action had not yet been taken.

Steps of the excessive deficit procedure provided for by article 104(9) and 104(11) do not apply to Hungary as it is not a member of the euro area.

The October 2006 Council recommendation set out measures for correction of the deficit by 2009, one year later than previously scheduled, with deficit targets of 10.1% of GDP for 2006, 6.8% for 2007, 4.3% for 2008 and 3.2% for 2009.

In view of economic downturn however, respecting the deficit target for 2009 is no longer regarded

as realistic. Hungary has requested assistance from international lenders, obtaining a EUR 6.5 billion loan from the EU in November 2008 as part of a EUR 20 billion package of assistance.

The Hungarian government now aims to correct its deficit in 2011, limiting the deterioration in 2009 to 3.9% of GDP, consolidating its budget with a 3.8% deficit in 2010 and reducing the deficit to 2.8% in 2011.

Given a higher-than-recommended structural adjustment achieved by Hungary since 2006 in a worse-than-expected macroeconomic environment, the Council is expected to find that Hungary has taken effective action and that a revised timetable for correction of its deficit is justified. In its recommendation, it is expected to call on Hungary to rigorously implement the necessary consolidation measures, starting in 2010.

#### Poland

The Council is expected to consider that special circumstances exist in the case of Poland, with a recession likely this year and fast rising unemployment rates. According to figures notified by the Polish authorities and validated by Eurostat, Poland's general government deficit reached 3.9% of GDP in 2008, thus exceeding the 3% reference value. And last month the Polish authorities announced that the deficit may significantly exceed the 4.6% of GDP planned for 2009.

In its recommendation, the Council is expected to call on Poland to ensure an annual fiscal effort of at least 1.25% of GDP, starting in 2010, so as to bring the deficit below 3% of GDP in 2012.

#### Romania

In the case of Romania, the Council is expected to consider special circumstances to exist, given large imbalances and the effect of the financial crisis on the country's economy. Romania requested assistance from international lenders in March, obtaining EUR 20 billion, including a EUR 5 billion loan from the EU. According to figures notified by the Romanian authorities and validated by Eurostat, the general government deficit reached 5.4% of GDP in 2008, thus largely exceeding the 3% reference value.

Romania's convergence programme (see following item) envisages a reduction of its government deficit from 5.4% of GDP in 2008 to 5.1% in 2009, thanks to consolidation measures undertaken in the 2009 budget adopted in February and additional measures taken in a rectified budget approved in April. It provides for further reduction of the deficit to 4.1% of GDP in 2010 and below 3% in 2011.

To achieve this, the Council is expected to call on Romania to ensure an average annual fiscal effort of at least 1.5% of GDP in structural terms, starting in 2010.

#### **Stability/convergence programmes - Belgium, Latvia, Austria, Romania, Slovakia, Slovenia**

The Council is due to adopt opinions, as required by the EU's stability and growth pact, on a number of annual updates of the member states' stability and convergence programmes.

The draft opinions relate to:

- updated stability programmes presented by Belgium ([doc. 9235/09](#)), Austria ([9157/09](#)), Slovakia ([9844/09](#)) and Slovenia ([9677/09](#));
- updated convergence programmes presented by Latvia and Romania ([doc. 11375/09](#)).

Under the stability and growth pact, member states having the euro as their currency are required to implement stability programmes, and those not participating in the single currency to implement convergence programmes. The aim is to ensure sound government finances as a means of strengthening the conditions for price stability and for sustainable growth, conducive to employment creation.

Based on article 99(5) of the European Community treaty, the opinions require a simple majority within the Council for adoption.

#### **Medium-term budgetary objectives - Implicit liabilities**

The Council, under "other business" will hold an exchange of views on the treatment of implicit

liabilities (such as pension schemes) in member states' national budgets, with regard to their medium-term budgetary objectives set under the EU's stability and growth pact.

**NovaRes Team**