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Macroeconomic Policy Advice and the Article IV Consultations:

A European Union Case Study

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Introduction

Europe remains mired in its second recession in three years, and the International Monetary Fund's (IMF's) most recent (October 2012) World Economic Outlook (WEO) sees its problems as perhaps the most important drag on world economic growth, which has slowed to a projected 3.3 percent for 2012 (as compared with 3.8 percent for 2011 and 5.1 percent for 2010). For Europe, the IMF notes that "[t]he baseline outlook for the region, weaker now than expected in the April 2012 WEO, is for further anemic growth or contraction in 2012 and a moderate pickup in growth in 2013. The possibility that the euro area crisis will escalate remains a major downside risk to growth and financial sector stability until the underlying issues are resolved" (2012a: p. 62-63).

Many economists, including Nobel Laureate Paul Krugman (2012), have argued that the policies implemented by the European authorities have helped push Europe into recession, and/or have been impeding the recovery. The IMF is part of the so-called "Troika" – with the European Commission (EC) and European Central Bank (ECB) that has been deciding or strongly influencing economic policy in the eurozone, as well as affecting policy in the rest of the European Union, especially since the world economic crisis and recession of 2008-2009. It is therefore worth examining IMF policy recommendations to see whether they have contributed to the ongoing crisis in Europe, and also how they might affect other European Union goals such as those of Europe 2020, which seeks to reduce social exclusion, promote public investment in research and development, and promote employment and education (European Commission 2012a).

The IMF makes policy recommendations to European countries through its Article IV consultations and resulting papers. These are the bilateral part of the IMF's surveillance responsibility; the IMF also does multilateral surveillance of the world economy, for example in its bi-annual World Economic Outlook, Global Financial Stability Report, and Fiscal Monitor. The IMF describes its surveillance function as follows:

"Surveillance in its present form was established by Article IV of the IMF's Articles of Agreement, as revised in the late 1970s following the collapse of the Bretton Woods system of fixed exchange rates. Under Article IV, member countries undertake to collaborate with the IMF and with one another to promote stability. For its part, the IMF is charged with (i) overseeing the international monetary system to ensure its effective operation, and (ii) monitoring each member's compliance with its policy obligations" (2012b).

The IMF's Article IV consultations provide recommendations on a broad range of issues including fiscal, monetary, and exchange rate policy; health care and pensions; labor market policy (including wages, unemployment compensation, and employment protections); and numerous other policy issues.

This paper examines the policy advice given by the IMF to European Union countries in 67 Article IV agreements for the four years 2008-2011 (IMF 2012c). It is a follow up to an ILO study on 50 Article IV agreements undertaken for low and middle-income countries (Islam et al. 2012). It focuses in particular on fiscal adjustments, inflation targeting (in countries where it is relevant, i.e. outside the eurozone), employment generation and social protection.

This content analysis finds a consistent pattern of policy recommendations, which indicates (1) a macroeconomic policy that focuses on reducing spending and shrinking the size of government, in many cases regardless of whether this is appropriate or necessary, or may even exacerbate an economic downturn; and (2) a focus on other policy issues that would tend to reduce social protections for broad sectors of the population (including public pensions, health care, and employment protections), reduce labor's share of national income, and possibly increase poverty, social exclusion, and economic and social inequality as a result.

Fiscal consolidation is recommended for all 27 EU countries, and expenditure cuts are generally preferred to tax increases. In some cases there are targets or limits on public debt/GDP ratios or fiscal deficits that are below those of the Maastricht treaty. There is repeated emphasis on cutting public pensions and "increasing the efficiency" of health care expenditures. Raising the retirement age is a standard recommendation, without any correlation to a country's life expectancy. Although slowing population growth can have important benefits (not the least of which is reduced pressure on the world's resources and climate change), an aging population is seen throughout these agreements as a threat to the fiscal sustainability of government expenditures. This is not demonstrated through empirical evidence, for example, which might take into account productivity growth that would support a rise in the ratio of retirees to workers, while allowing for rising living standards for both, as has been the case in prior decades. There also appears to be a predilection for increasing labor supply, irrespective of unemployment or labor force participation rates. This includes such measures as reducing eligibility for disability payments or cutting unemployment compensation, as well as raising the retirement age.

Labor market policy recommendations are overwhelmingly geared towards measures that would either reduce wages directly or – as in the efforts to increase the labor force – put downward pressure on wages. Such measures include the attenuation of industry-wide bargaining practices, and scaling back employment protections.

The paper's findings are also consistent with other evidence of policy mistakes, including that provided by IMF research. On the macro-economic side, the IMF's most recent WEO finds that the IMF (as well as other forecasters) seriously under-estimated government spending multipliers in growth forecasts for countries since the beginning of the Great Recession. Instead of a multiplier of 0.5, they find a range of 0.9 to 1.7 (2012a: p. 41-43). This could explain some of the large gap between the IMF's growth projections and growth outcomes for countries undergoing fiscal consolidation under IMF agreements. For example, in September 2010 the IMF projected GDP growth in Greece of -2.6 percent for 2011 and +1.1 percent for 2012. The actual results were -6.9 percent for 2011 and - 6 percent (October WEO projection) for 2012 (Weisbrot and Montecino 2012). Similarly, in Latvia the IMF projected, in January of 2009, -5 percent growth for 2009; the actual decline was 18 percent (Weisbrot and Ray 2010).

It is worth noting that recent IMF research provides evidence for a more nuanced approach to fiscal consolidation. Perhaps most importantly, an IMF Staff Discussion Note published last June (Barkbu et al. 2012) expresses a number of serious concerns about how lagging growth since the Great Recession "has pressured already deteriorated fiscal positions and public debt dynamics, and increased unemployment, particularly in the Southern euro area countries..." (p. 5). While supporting many of the structural reforms recommended in the Article IV consultations, and also favoring fiscal consolidation, the paper notes that a "distinct threat is that, in an environment of weak aggregate demand, supply-side measures and restructuring fail to boost output, leaving part of Europe in a period of protracted stagnation" (p. 8). It offers examples of how, in the absence of sufficient aggregate demand, the proposed structural reforms could go bad: "relaxing employment protection may not stimulate hiring in the short term, but increase unemployment. Similarly, reducing unemployment insurance or increasing the retirement age would lower disposable income if those induced to seek work do not find jobs... Furthermore, because persistent weak demand can negatively impact long-run prospects through hysteresis effects in unemployment, it is imperative to increase growth soon" (p.17).

Similarly, an empirical Working Paper by Batini et al (2012) draws the following conclusions, among others:

> *Implementing fiscal consolidations during periods of positive output growth reduces significantly the impact on output;*
>
> *If consolidations need to be implemented during downturns (for instance, to regain market confidence), they should prioritize increases in net taxes…*
>
> *If consolidations have to occur during downturns and prioritize cuts in public consumption and investment, they should be smooth and gradual and be accompanied by increases in net taxes* (p.8).

A 2009 examination of IMF agreements and reviews made during the Great Recession, with 41 borrowing countries, found that 31 recommended pro-cyclical fiscal or monetary policies, or (in 15 cases) both (Weisbrot et al. 2009). These were policies that could be expected to exacerbate a significant slowdown or recession. In that study, there were many cases in which the IMF's pro-cyclical policies were based on overly-optimistic assumptions about economic growth. For example, of the 26 countries that had at least one review, 11 IMF reports had to lower previous forecasts of real GDP growth by at least 3 percentage points, and three of those had to correct forecasts that were at least 7 percentage points overestimated.[1]

Pro-cyclical fiscal policies have also played a major role in the deep recessions experienced by Spain, Italy, Portugal, and Ireland. The IMF's role, together with the European authorities, in promoting these policies, is only partially reflected in the Article IV papers reviewed below. But the "one-size fits all" policy of fiscal consolidation that is evident in these Article IV consultations is consistent with what the IMF recommended in borrowing countries in the eurozone.

There are also a number of references to the idea that crises present an opportunity to make changes that might otherwise be difficult. In Spain's 2010 Article IV consultation, for example, IMF staff argued that "empirical evidence also suggests that recoveries from economic crises often serve as an opportunity for reform" (p. 13). These statements, combined with the consistency of the IMF's

1 The content analysis below only looks at Article IV papers, so it does not fully capture many of the IMF's worst macroeconomic policy outcomes in Europe. That is because countries such as Greece, Portugal, and Latvia – although they are included below because they had at least one Article IV consultation between 2008-2011, did not always have regular Article IV consultations while they were operating under IMF lending agreements; although they did have reviews of their agreements, which are not examined in this paper. For example, Greece has had enormously pro-cyclical fiscal policies under IMF agreements, cutting spending by a full 8.7 percent of GDP during 2010-2011, with more tightening for 2012 and beyond, and the economy still shrinking.

recommendations and lack of correlation with the specific conditions of the countries, indicate a policy agenda that suggests a 'one-size-fits-all' approach.

Over the past two and a half years, as the crisis in the eurozone has unfolded, the European authorities have repeatedly intervened –even including ECB interventions or pledges to intervene in sovereign bond markets – in order to stabilize financial markets and prevent the crisis from worsening at various times, even while promoting pro-cyclical policies that have prolonged recession. However, there have been numerous press reports indicating[2] that these authorities, including the ECB, were unwilling to take further measures to end the crisis because of a fear that doing so would remove the pressure on eurozone governments to make certain reforms (Jones and Suoninen 2012; Fontanella-Khan 2012).[3] It is possible that the current recession and recurring crises in Europe are a result of this attempt to implement unpopular reforms in various countries – especially since the ECB has several times shown that it can easily limit, and lower interest rates on the sovereign bonds of Italy and Spain when it wants to do so.

The Article IV consultations examined in this paper provide an important picture of the reform agenda that the European authorities are looking for in their interactions with countries in the European Union. For this reason they deserve careful analysis and scrutiny.

Methodology

This content analysis reviewed 67 IMF Article IV consultations with EU countries from January 1, 2008 to December 31, 2011 (See Appendix A for a full list of consultations). For countries, that had entered lending arrangements, consultation reports were not necessarily available. The policy recommendations reviewed were for the medium term, typically a two to five year timeframe following the consultation. When possible, the IMF's own determination of the medium term recommendations in the reports was used. In the analysis, we defined a policy recommendation to be a recommendation that was new or went beyond policies that were being implemented or planned to be implemented by the country's authorities.

The content analysis focused on four areas of economic and social policies: fiscal policies, inflation targeting, labor market policies, and social policies, including education, pensions, health and welfare. The analysis consisted of four steps. The first step of the analysis identified policy recommendations made in a given consultation report. Second step coded the policy recommendation under variable category. To minimize potential biases in the characterization of a

2 "France and Italy piled more pressure on the European Central Bank on Tuesday to agree to steps this week to reduce crippling borrowing costs for southern eurozone states. But the bank is expected to outline rather than detail its strategy on Thursday in order to keep the pressure on politicians to bring their deficits and debts under control. …. [ECB executive board member Joerg Asmussen, the most senior German at the IMF] said it was crucial to ensure that ECB decisions did not reduce pressure on governments to reform. That is one reason why the central bank is unlikely to reveal all details of the plan on Thursday."

3 "Mario Draghi, ECB president, last week said the bank would do 'whatever it takes' to safeguard the euro, fuelling investors' hopes that the central bank would buy Spanish and Italian bonds in an effort to bring borrowing costs under control. But senior eurozone officials have damped such hopes, suggesting that the ECB will seek further guarantees of reform before assisting debt-ridden countries."

recommendation, the third step linked the recommendation to a quote for the country summaries in section 6. In the final step, a review of the quotes was conducted to assess whether they were taken in or out of context.

Fiscal adjustment

The IMF Article IV consultations with EU countries typically centered on fiscal adjustment and financial security. Fiscal adjustment to reduce the government primary budget deficit is attained from a reduction in government expenditures, an increase in tax revenues, or a combination of both. The goals of fiscal adjustment identified by the IMF were fiscal sustainability, credibility, and reducing uncertainty. The content analysis reviewed recommendations for identified government expenditure and debt targets, the expenditure-revenue composition of consolidation, and specific measures proposed. The explicit spending restraint variable is defined as the IMF recommendation for explicit control or cuts in public spending (see **Table 1**). Measures ranged from reducing public sector employment to expenditure ceiling to social reforms. The public sector debt variable is defined to include recommendations to rein in the public debt. The revenue mobilization variable is defined to include aspects of tax and non-tax revenue reforms.

TABLE 1
Examples of the Types of Fiscal Adjustment Recommendations

Category	Recommendation	Reference
Fiscal Consolidation	"once the current crisis is past, the fiscal stance will have to be significantly tightened to achieve long-run stability"	Belgium 2008: 4
Expenditures	"introducing a cap on total expenditure growth for each level of government and the social security administration"	Belgium 2009: 20
Expenditures	"containing public wage growth"	Bulgaria 2010: 5
Debt	"to put the government debt-to-GDP ratio on a downward path"	Hungary 2008: 3
Revenues	"much of the adjustment effort may need to fall on the revenue side"	Estonia 2009: 4
Taxes	"phasing out exemptions and deductions; taxing the self-employed and the informal sector"	Greece 2009: 24
Other revenues	"Ireland has scope for raising social security contributions"	Ireland 2009: 27

Source: Various IMF Article IV Consultations, 2008-2011.

Inflation targeting

The inflation targeting variable is defined as recommendation for inflation targeting. The content analysis looked at recommendations on specific inflation targets, interest rates, exchange rates, and other inflation control measures (see **Table 2**). Inflation targeting recommendations were reviewed only for EU countries which had not adopted the euro as currency. The content analysis included both short-term as well as medium-term recommendations on inflation targeting, as the IMF consultation reports typically did not differentiate between the two. Inflation targeting recommendations did not feature prominently in the consultations, and were often not discussed. This might in part be due to most EU countries experienced a slowing of inflation during the period of study due to the recession, and thus inflation was in most cases not a concern. In the case of Finland, the 2010 consultation report noted, "inflation is likely to decline as a sizable output gap strengthens resistance to price and salary increases" (p. 14).

Furthermore, inflation concerns were expressed in several of the consultations with countries in the eurozone that had above-average inflation. Labor market policies of increasing labor force participation and wage restraint were proposed as effective tools to combat inflation, and these are further discussed under labor market policies.

TABLE 2
Examples of the Type of Inflation Targeting Recommendations

Category	Recommendation	Reference
Meeting target	"monetary policy should aim to reduce CPI inflation to the 3 percent target"	Hungary 2008: 3
Interest rates	"further gradual hikes in the policy rate… would bring inflation back to the 2½ percent target"	Poland 2011: 11
Expectations	"tight monetary policy and subdued growth will be required to prevent elevated inflation expectations"	United Kingdom 2008: 22
Non-specific	"boosting competition requires bringing inflation down"	Romania 2010: 25

Source: Various IMF Article IV Consultations, 2008-2011.

Labor force and employment expansion

The labor force variables are defined to include references to expansion of labor force expansion and employment generation (see **Table 3).** The analysis looked at measures to increase labor supply, labor demand and labor market flexibility. The consultations often suggested increased labor market flexibility, including scaling back employment protections, lowering severance pay, and decentralizing collective bargaining, rather than employment protection. Labor supply measures included training, reducing unemployment benefit, and increasing the retirement age. Labor demand focused on wage moderation.

TABLE 3
Examples of the Types of Labor Market Policy Recommendations

Category	Recommendation	Reference
Wages	"even though in the medium term eliminate wage indexation remains necessary,…"	Luxembourg 2011: 17
Employment protection	"further liberalization of employment protection legislation is necessary in the medium term"	Slovenia 2009: 12
Labor supply	"with concerns about unemployment easing, labor market policies should re-focus on looming labor supply pressures"	Denmark 2010: 31
Labor market flexibility	"… labor market flexibility should remain policy priorities"	Slovakia 2009: 16
Employment	"curtailing public sector employment by not replacing a sizeable share of retiring public servants"	Belgium 2011: 37
Unemployment benefits	"limiting the level of unemployment benefits over time or their duration"	Belgium 2009: 22
Training	"foster development of human resources in technical fields"	Estonia 2011: 17

Source: Various IMF Article IV Consultations, 2008-2011.

Social policies

The education variable is defined as recommendations on primary, secondary and higher education, as well as training and apprenticeship programs. Other social policy variables are defined to include any reference to social transfers, old-age pensions, health care, child benefits and anti-poverty programs (see **Table 4**). The topics of poverty, social exclusion and income security were rarely addressed in the consultations reviewed. Social policy recommendations were often made in the context of fiscal consolidations, and overwhelmingly focused on scaling back coverage and benefits. A recurrent theme in the consultation was the aging of the population and resulting pressures on public expenditures on pensions and health care.

TABLE 4
Examples of the Types of Social Policy Recommendations

Category	Recommendation	Reference
Education	"improving… the quality of education"	Czech Republic 2010: 6
Social benefits	"consideration should also be given to… the indexing of benefits to more appropriate price baskets"	Ireland 2009: 26
Pension	"legislating additional future increases in the retirement age (especially for women)"	Italy 2008: 25
Health care	"savings require… (ii) additional efforts to rein in health care expenditures"	Netherlands 2008: 24
Disability and others	"tighten eligibility for child, disability and sickness benefits, and decrease the term of maternity benefits to international levels"	Lithuania 2009: 14
Welfare	"reforms to strengthen the targeting of transfer programs and tighten eligibility"	Slovenia 2009: 9
Poverty	"social support measures should be targeted to reach the truly needy"	Cyprus 2009: 17

Source: Various IMF Article IV Consultations, 2008-2011.

A method of coding of variables was then followed to identify if the IMF consultation recommended and referred to a certain policy. Specific key terms were identified, and sentences that capture the incidence of a particular form of policy advice were also taken into account. A variable was coded 1 = "increase" if an increase or expansion in policy A is recommended for country X; 2 = "decrease" if a decrease or contraction in policy A is recommended for country X; N = "neutral" if the recommendation neither increased nor decreased policy A, or it could not be determined from the information provided; and 0 = "no" if policy A is not recommended.

Comparative Overview

The content analysis examined the fiscal policy recommendations offered in IMF Article IV consultations from 2008 to 2011. During this period, the European Union entered an economic recession. As shown in **Table 5**, some countries were more severely impacted with sharp and/or sustained contraction in the economy (including Estonia, Greece, Latvia, and Lithuania), while other countries recovered fairly quickly (including Germany, Poland, and Sweden). The IMF consultations provided both short-term economic advice addressing the immediate economic crisis as well as medium to long-term advice for fiscal adjustment. The content analysis focused primarily on the medium-term recommendations.

TABLE 5
Real GDP Growth (Annual Percent Change) for EU Countries, 2008-2011

EU Country	2008	2009	2010	2011
Austria	1.4	-3.8	2.1	2.7
Belgium	1.0	-2.8	2.4	1.8
Bulgaria	6.2	-5.5	0.4	1.7
Cyprus	3.6	-1.9	1.1	0.5
Czech Republic	3.1	-4.7	2.7	1.7
Denmark	-0.8	-5.8	1.3	0.8
Estonia	-3.7	-14.3	2.3	7.6
Finland	0.3	-8.5	3.3	2.7
France	-0.1	-3.1	1.7	1.7
Germany	0.8	-5.1	4.0	3.1
Greece	-0.2	-3.3	-3.5	-6.9
Hungary	0.9	-6.8	1.3	1.7
Ireland	-2.1	-5.5	-0.8	1.4
Italy	-1.2	-5.5	1.8	0.4
Latvia	-3.3	-17.7	-0.3	5.5
Lithuania	2.9	-14.8	1.4	5.9
Luxembourg	0.8	-5.3	2.7	1.6
Malta	4.1	-2.6	2.5	2.1
Netherlands	1.8	-3.7	1.6	1.1
Poland	5.1	1.6	3.9	4.3
Portugal	0.0	-2.9	1.4	-1.7
Romania	7.3	-6.6	-1.6	2.5
Slovakia	5.8	-4.9	4.2	3.3
Slovenia	3.4	-7.8	1.2	0.6
Spain	0.9	-3.7	-0.3	0.4
Sweden	-0.8	-5.0	5.9	4.0
United Kingdom	-1.0	-4.0	1.8	0.8

Source: International Monetary Fund, *World Economic Outlook, October 2012: Coping with High Debt and Sluggish Growth*. Washington, DC, October 2012: Table A2. Advanced Economies: Real GDP and Total Domestic Demand, p. 191; and Table A4. Emerging Markets and Developing Economies: Real GDP, p. 194.

In a number of consultations, IMF staff argued that the economic crisis provided an opportunity for economic reforms. For example, in the 2009 consultation report with France, IMF staff wrote that "historical experience indicates that successful fiscal consolidations were often launched in the midst of economic downturns or the early stages of recovery"[4] (p. 20). In other country cases, IMF staff made the case that the economic crisis created a necessity for fiscal consolidation. For example, the 2010 consultation with the Czech Republic stated "the crisis has highlighted the urgency of fiscal

4 The IMF report did not provide a reference for this claim. Here, it is worth citing that the IMF's research argues the opposite, that is, fiscal consolidation is best undertaken during normal periods of growth and that consolidation exercises should be carefully sequenced. Perhaps this is the reason why, by 2011, the IMF noted (in the case of Netherlands), that "historical experience indicates that negative effects on demand from budget consolidation are likely to be higher when monetary policy is not able to accommodate tightening, as is currently the case" (p. 21).

adjustment" (p. 4). Only a few consultations directly discussed the contractionary effects of proposed fiscal consolidation. For example the 2010 consultation with the United Kingdom noted that "although this consolidation effort involves painful decisions and dampens short-run growth, it is necessary to enhance credibility and ensure fiscal sustainability" (p. 26).

Fiscal policies

The IMF consultations advised fiscal consolidation for each of the 27 EU countries. The consultations generally emphasized expenditure cuts over revenue increases. In the 2010 consultation with Latvia, IMF staff stated that "international experience suggests expenditure cuts, particularly current spending, generate more sustainable adjustment" (p. 29). The 2011 consultation with the Netherlands furthermore noted that "expenditure-based consolidations have generally been more successful, based on international evidence" (p. 25). The 2009 consultation with the Republic of Ireland found that "large fiscal adjustments that focused on expenditure cuts—particularly the wage bill and social transfers— have been better sustained than tax-based consolidations and have often been expansionary rather than contractionary" (p. 26).[5]

An expenditure ceiling was proposed for some countries to rein in government spending. For example in the 2010 consultation with the Republic of Ireland, IMF staff noted that "a medium-term fiscal framework incorporating expenditure ceilings is a valuable management tool" (p. 27). Most consultations provided specific recommendations on expenditure reductions, and in nearly all cases included reduction in social programs (see subsection below on social policies). Other areas frequently identified for consolidation were the slowing of wage growth in the public sector, public sector wage ceilings, reducing public sector employment, and reorganizing public institutions.

Figure 1 shows that expenditure decreases were recommended in consultations with most of the EU countries reviewed (96.3%). The most commonly recommended measures to rein in expenditures related to pensions. The IMF recommended reduction in pension spending from current level or projected level in consultations with 81.5 percent of countries. On the other hand, revenue increases were recommended in 70.4 percent of countries. In two-thirds of the countries in which revenue increases were recommended, the IMF also recommended revenue decreases. The IMF did not provide recommendations on government revenue in consultations with 25.9 percent of the countries.

The IMF consultations identified various areas for revenue increases including taxes, deductions, and social security contributions. Tax policy recommendations were country specific and often included a mixture of increases and reductions in taxes. For example, the 2008 consultation with Hungary proposed "shift in the tax burden away from labor and to consumption and wealth" (p. 3). Based on the information provided in the consultation reports, the net revenue effect could not be determined in most consultations. Tax areas identified for revenue enhancement included income taxes, property taxes, inheritance taxes, value added tax (VAT), reducing or phasing out the mortgage interest deduction, and phasing out other deductions, exemptions and loopholes. For example, in the 2011 consultation, Italy was advised to "reduc[e] tax evasion" (p. 1). The 2009 consultation with Greece recommended "phasing out exemptions and deductions; taxing the self-employed and the informal sector" (p. 24).

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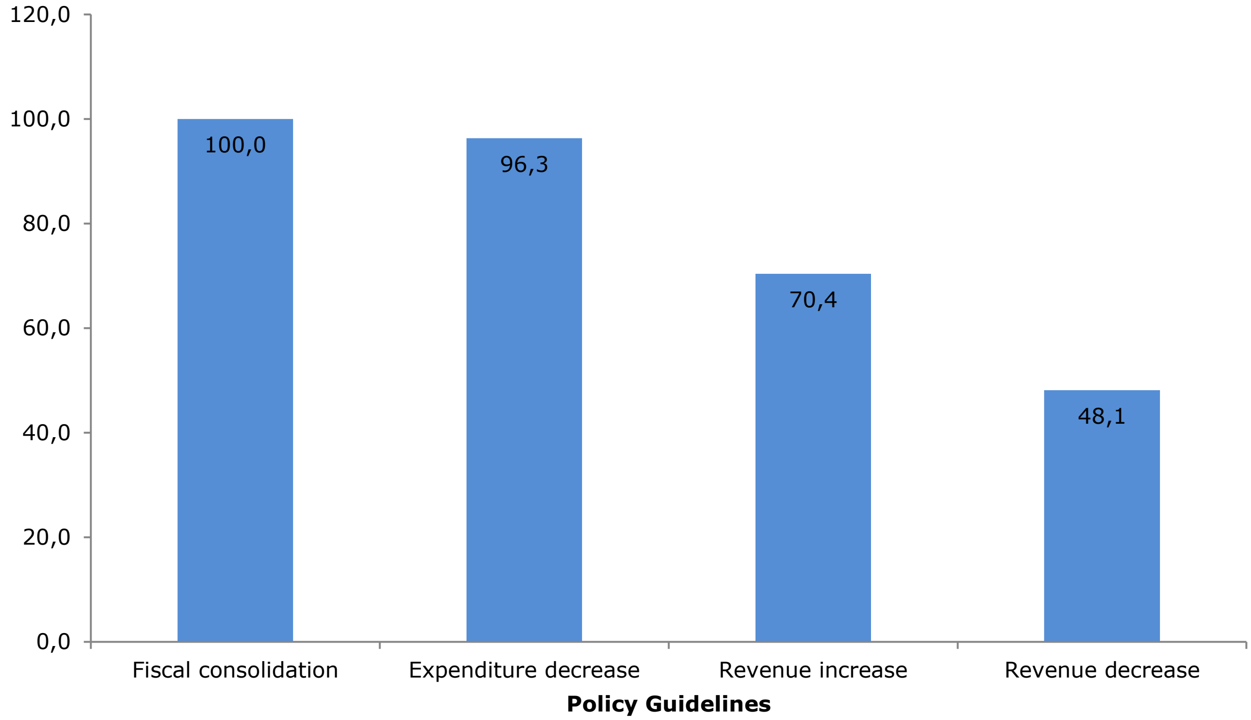
5 The IMF did not provide a reference for this claim in any of the reports mentioned. See above.

FIGURE 1
Country Frequency of Fiscal Policy Recommendations for EU Countries, 2008-2011 (in percent)



Source: Various Article IV consultation reports with EU countries, 2008-2011. Note: The IMF recommended both revenue increases and revenue decreases in consultations with 10 countries. The net revenue effect could not be determined based on the information provided in the consultation reports. The IMF did not provide revenue recommendations in consultations with 6 countries.

In the case of some countries, the IMF determined that tax levels were too high, and advised lowering taxes. For example, in the 2011 consultation with Germany, IMF staff wrote that "recent studies find that among all taxes, corporate taxes are the most harmful to economic growth"[6] (p. 28).

In a number of consultations, specific budget deficit or debt targets were identified. In some cases, the IMF staff recommended stricter targets than the ceilings set by the Stability and Growth Pact. For example, the 2011 consultation with Hungary stated "the constitutional mandate to maintain public debt below 50 percent is commendable" (p. 16). IMF staff found "the current fiscal rules -- targeting a surplus of 1 percent of GDP across the cycle, supported by medium-term expenditure ceilings – remain[ed] well suited for Sweden" in the 2010 consultation (2010: 36). Few consultations reviewed expressed concerns about planned fiscal consolidation. The consultation with Poland warned that "aiming at a deficit of 3 percent already by 2012 is too ambitious" (p. 18). While the 2011 consultation with the Netherlands supported the authorities' planning consolidation but cautioned that "historical experience indicates that negative effects on demand from budget consolidation are likely to be higher when monetary policy is not able to accommodate tightening, as is currently the case" (p. 21). Finally, in the 2011 consultation with Slovenia, IMF staff determined the public debt level to be sustainable, but still recommended fiscal consolidation: "While general

6 No references were provided. See above

government debt is likely to remain sustainable, fiscal consolidation is necessary in light of the uncertainty in financial markets and contingent liabilities" (p. 8).

Inflation targeting

The IMF consultations offered inflation targeting advice to five non-euro countries (see **Table 6**). The recommendations were to tighten monetary policy to bring inflation within the established target (for example Poland 2011), or lower the inflation target itself (Czech Republic 2008). Only one consultation discussed controlling inflation in detail. The UK consultation report for 2008 discussed "a monetary stance that remains focused on the inflation target;" (p. 4) and "tight monetary policy and subdued growth will be required to prevent elevated inflation expectations from getting embedded into wages and prices" (p. 22). Two years later, the 2010 consultation expressed concerns over disinflation. "If a stalling recovery were to heighten disinflationary forces, quantitative easing should be expanded" (p. 37).

TABLE 6
IMF Policy Recommendations on Inflation Targeting, and Average and Projected Inflation for Non-Euro EU Countries, 2008-2011

	Avg. Inflation 2008-11	Projected Inflation 2015	Inflation Targeting Recommendation
Bulgaria	2.7	3.0	
Czech Republic	2.7	2.0	1, 2
Denmark	2.4	2.0	
Hungary	4.5	3.0	1
Latvia	1.9	2.2	
Lithuania	2.7	2.4	
Poland	3.3	2.5	1,2
Romania	4.5	2.6	
Sweden	1.8	2.0	1

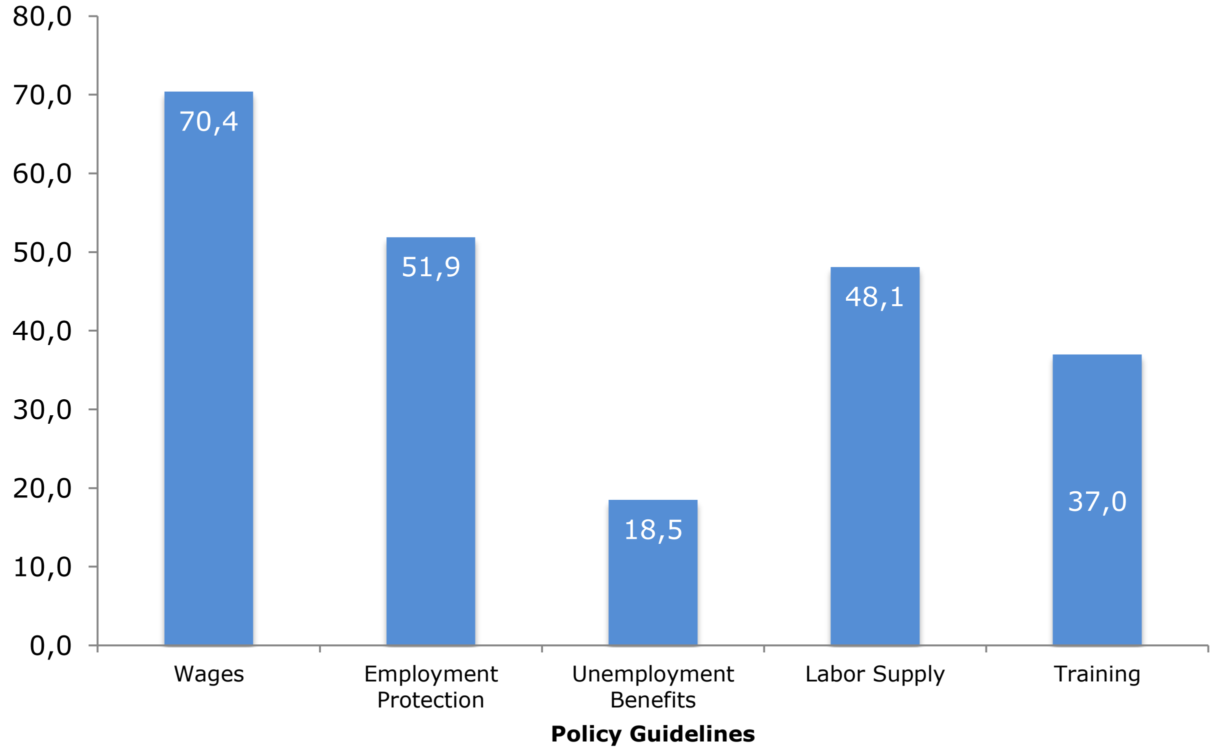
Source: International Monetary Fund, World Economic Outlook tables, inflation average consumer prices, percent change; and various Article IV consultation reports with EU countries, 2008-2011. Note: "1" denotes in tightening/lowering of inflation targeting, while "2" denotes a loosing of inflation targeting.

Labor market policies

The majority of the consultations reviewed addressed labor market policies. The content analysis uncovered five main areas of labor market recommendations: Wages, employment protection and flexibility, collective bargaining, work incentives, and vocational training. During the period of this study, unemployment rose in the EU countries as the recession took hold. Some countries were impacted more than others due to the severity of the recession and their specific labor market structure. By 2010, the unemployment rate ranged from 4.4 percent in Austria to 20.1 percent in Spain (see **Table 7**).

Figure 2 summarizes the country frequency of recommendations on wages, employment protection, unemployment benefits, labor supply/labor force participation, and vocational training. For the majority countries, the IMF provided recommendations on wage growth, and the advice overwhelmingly favored wage moderation (18 out of 19 countries). The IMF provided advice on labor supply and/or labor force participation with 48.1 percent of countries. In every case, the advice promoted policies increasing labor supply. Finally, IMF recommended scaling back employment protections in 14 out of 14 countries receiving advice on employment protection. In consultations with 7 countries, advice on vocational training and apprenticeship programs supplemented recommendations on weaker employment protection.

FIGURE 2
Country Frequency of Labor Market Policy Recommendations for EU Countries, 2008-2011 (in percent)



Source: Various Article IV consultation reports with EU countries, 2008-2011.

In 2007, IMF staff stated in their consultation with France that "labor market rigidities are probably the single most significant barrier to higher economic growth and employment" (p. 10). Increases in labor market flexibility through scaling back of employment protection, decentralizing collective bargaining, flexibility in overtime and workweek hours were mentioned in consultations with 15 countries. For example, the 2010 consultation with Germany advised "further increasing labor market flexibility through decreasing both legal and labor-court based employment protection" (p. 27). The IMF consultations did not promote the concept of flexicurity adopted by Denmark and promoted in the Europe 2020 Strategy. Only the 2009 consultation with Slovenia made the case for "further liberalization of employment protection legislation… could be implemented in the context of a 'flexicurity' approach"[7] (p. 12). On the other hand, consultations with Italy (2008), the Netherlands (2008), and Belgium (2009) advised reducing income security by scaling back on unemployment benefits level and/or duration of benefits.

7 The 2009 consultation with Cyprus proposed flexicurity as an option in the public sector.

To increase employment, IMF consultations for 18 countries advised reducing nominal or real wage growth (Figure 2). Specific recommendations included reducing or eliminating cost of living adjustments (COLA) (for example see Cyprus 2009), wage modification in collective bargaining (see Sweden 2011), minimum wage moderation (see France 2009), and containing public sector wage growth. The 2010 consultation with Bulgaria speculated that "containing public wage growth… [would] also help limit economy-wide wage growth and help competitiveness" (p. 19).

TABLE 7
Labor Force Participation Rate, Unemployment Rate, 2010, and Incidence of IMF Recommendations on Labor Supply and Employment Protection Policies for the EU Countries, 2008-2011

EU Country	Labor Force Participation Rate 2010	Policy Guidelines for Labor Supply Expansion	Unemployment Rate 2010	Policy Guidelines for Employment Protection
Austria	75.1	1	4.4	2
Belgium	67.7	1	8.3	2
Bulgaria	66.5		10.2	
Cyprus	74.4		6.5	
Czech Republic	70.2	1	7.3	2
Denmark	79.4	1	7.4	
Estonia	73.8	1	16.9	2
Finland	n/a	1	8.4	
France	70.5	1	9.7	2
Germany	76.6	1	7.1	2
Greece	68.2		12.6	2
Hungary	62.4	1	11.2	
Ireland	69.8		13.7	
Italy	62.2	1	8.4	
Latvia	73.2		18.7	
Lithuania	70.5		17.8	2
Luxembourg	68.2		4.5	
Malta	60.3		6.8	2
Netherlands	78.2	1	4.5	2
Poland	65.6	1	9.6	
Portugal	74.0		11.0	
Romania	63.6	1	7.3	
Slovakia	68.7		14.4	2
Slovenia	71.5		7.3	2
Spain	73.4		20.1	2
Sweden	n/a		8.4	2
United Kingdom	75.5		7.8	

Sources: ILO, LABORSTA, Short Term Indicators of the Labour Market, Indicator, Labor Force Participation Rate, ages 15-64 years; Unemployment Rate, ages 15-74 years; and various IMF consultation reports for EU countries, 2008 to 2011. Note: "1" denotes a recommended increase or expansion of policy, e.g. increase in labor supply or expansion of employment protection; and "2" denotes a recommended decrease/contraction of policy. In eight additional consultations (not included), increasing labor force participation was not discussed explicitly, but the consultations included recommendations which would have a positive effect on labor force participation, such as increasing the retirement age.

The labor force participation rate varied widely across EU countries, with Malta (60.3%), Italy (62.2%) and Hungary (62.4%) having the lowest rates and Denmark having the highest rate (79.4 percent) (see **Table 7**). Twenty-two consultations with 13 countries recommended increasing labor force participation/labor supply. For example, the 2010 consultation with Denmark recommended that "labor market policies should re-focus on looming labor supply pressures," despite a near doubling in the unemployment rate over just one year (p. 22). Consultations with an additional eight countries did not explicitly discussed increasing labor force participation or labor supply, but the consultations included recommendations which would have a positive effect on labor force participation, such as increasing the retirement age. An increase in labor force participation is believed to increase potential output and reduce wage pressure. The 2009 consultation with Belgium made the case for "further labor market reforms [being] essential for increasing the labor supply and potential output, as well as for supporting job creation." Specific labor market recommendations for Belgium included enhancing monitoring of job search activities, increasing job counseling, applying penalties for refusal of suitable jobs, raising the effective retirement age, equalizing women's retirement age to that of men, phasing out early retirement schemes, and tightening eligibility for disability benefits.

Interestingly, there was no apparent correlation between a country's labor force participation rate and recommendation to increase the labor force. Bulgaria and Malta had some of the lowest labor force participation rates in EU, but the IMF did not provide specific advice on increasing the labor supply in the consultations reviewed.[8] At the same time, the IMF recommended increases in labor supply for Austria, Denmark, Germany, and the Netherlands, countries which had some of the highest labor force participation rates. Likewise, recommendations to increase labor force participation were not obviously correlated with the countries' unemployment rates either.

Social Policies

The consultations provided few specific recommendations on education. When recommendations were made, they were often brief and generic in nature, such as "improve quality of education" (Bulgaria 2010, Czech Republic 2010, Italy 2011, Latvia 2010). The content analysis identified seven country-specific recommendations on primary, secondary and higher education in seven consultations with seven countries. Some of the recommendations focused on investment in education to increase human capital. Other recommendations were geared toward reducing expenditures. For instance, the 2009 consultation with Austria identified four key areas for consolidation including education (p. 32). The 2009 Lithuania consultation noted that there was "scope for savings in the education sector" (p. 14).

Many EU countries experienced high unemployment during the period of study, and vocational training and apprenticeship training programs were proposed in consultations with ten countries to reduce mismatches in the labor market. The 2011 consultation with Estonia noted that "despite double-digit unemployment, skill mismatches and job opportunities [outside the country] have resulted in labor shortages," and it found "the authorities' ongoing efforts to harmonize vocational education with the needs of the labor markets… are welcome" (p. 16). In several cases, vocational training was advocated in combination with increased flexibility. For example, the 2011 consultation

8 The 2008 consultation with Bulgaria did review policies implemented by authorities to increase labor force participation.

with Slovakia mentioned "sharpening the orientation of education and vocational programs towards labor market needs," while at the same time promoting labor market flexibility to maintain competiveness (p. 25).

EU countries have some of the highest life expectancies in the world (see **Table 8**). Long life expectancies combined with low birth rates have resulted in an "aging of population" in EU countries. The aging population was a recurrent theme in the IMF consultations with EU countries. Most consultations reviewed explicitly addressed the economic ramifications from an aging population in terms of pension and health care expenditures. For example, the 2011 consultation with the Netherlands emphasized "the priority should be reducing the impact of aging on fiscal expenditures (p. 25).

TABLE 8
Life Expectancies at Birth, 2010, and Incidence of IMF Recommendations on Pension and Health Care Policies for EU Countries, 2008-2011

Country	Life expectancy (in years)	Pension	Health Care
Austria	80	2	2
Belgium	80	2	2, N
Bulgaria	74	2	2,N
Cyprus	79	2	
Czech Republic	77	2	2
Denmark	79	2	
Estonia	75		
Finland	80	2	2
France	81	2	2
Germany	80	2	2
Greece	80	2	
Hungary	74	2	2,N
Ireland	80		
Italy	82	2	
Latvia	73	2	
Lithuania	73	2	2
Luxembourg	80	2	N
Malta	81	2	
Netherlands	81	2	2
Poland	76	2	
Portugal	79		
Romania	73	2	2
Slovakia	75		2
Slovenia	79	2	
Spain	82	2	2
Sweden	81		
United Kingdom	80	2	2

Source: World Bank, Data Indicator, Life expectancy at birth, total (years); and various IMF consultation reports for EU countries, 2008 to 2011. Note: "1" denotes a recommended increase or expansion of policy, "2" denotes a recommended decrease or contraction of policy; and "N" denotes either neutral or could not be determined from the information provided.

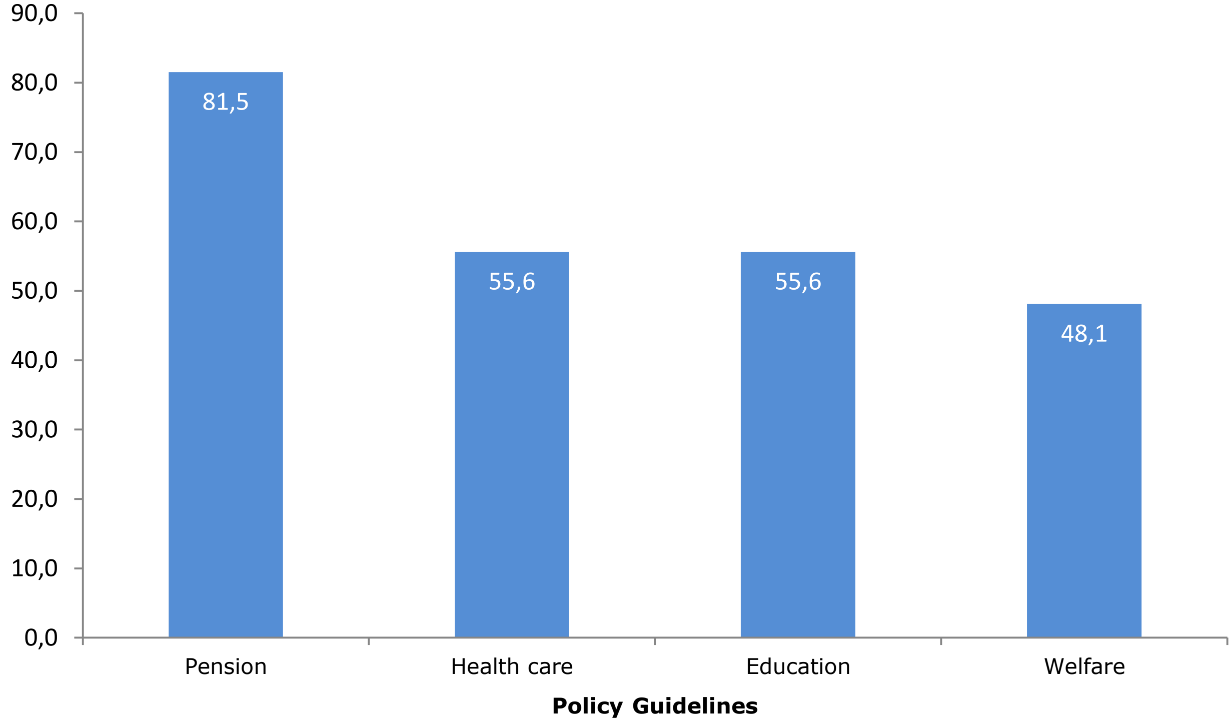
The IMF offered advice on pensions for 22 out of 27 countries reviewed. Pension recommendations were frequently referenced in the context of fiscal consolidation and focused on reducing pension spending in every single case. For example, the 2010 consultation report with Poland noted that "the substantial fiscal adjustment needed over the medium term will require changes in entitlement programs" (p.19). The 2009 Austrian consultation identified "key areas for consolidation to include… pensions, and education and health" (p. 32). Without exception, the pension recommendations focused on scaling back programs by tightening eligibility, raising retirement ages, increasing service period, reducing benefits levels (often through tightening pension indexation), and phasing out early retirement programs. Several consultations advocated expansion of private pensions to supplement cuts in public pension. For example, the 2011 consultation with Slovenia noted "the private pillar should be expanded to compensate for the public benefit cuts" (p. 9). The 2010 Romanian consultation suggested that Romania "build up the pillar two private pension system" (p. 22). While the 2010 consultation with the Czech Republic recommended going a step further by "moving to a fully funded second-pillar private pension scheme" (p. 5).

Interestingly, there did not appear to be a correlation between life expectancy and recommendations to scale back pension programs (see Table 8). The Republic of Ireland and Sweden had some of the highest life expectancies, but reviewed consultations did not provide recommendations on increasing retirement age. On the other hand, consultations with Hungary and Lithuania, countries with some of the lowest life expectancies at birth, recommended increasing the retirement age and/or reducing benefit levels.

A total of 26 consultations for 15 countries explicitly mentioned health care policies. As in the case of pensions, health care policy advice was frequently framed in terms of budget consolidation. For instance, the 2008 consultation with Germany warned of "the risks associated with healthcare costs due to an aging population" (p. 28). Generally, the health care policy recommendations were generic in nature, such as "continued efficiency gains… in health and long-term care spending" (France 2011: p. 21); "the large efficiency gains that are possible in the health care sector should be promptly reaped" (Austria 2011: p. 9); and "a comprehensive health care reform, with the view to improve the efficiency and quality of the health care system is needed" (Bulgaria 2010: 18). One exception was the 2010 Czech Republic consultation report, which offered specific recommendations to "reduce the broad coverage of publicly provided and insured services and allow greater scope for private sector provision of health services;" and "introduce voluntary insurance, personal health accounts, and choices in health benefits plans" (p. 6).

Figure 3 shows the country frequency for various social policy areas. Social policy recommendations included both recommendations for expansion of social programs as well as shrinking programs. The IMF consultations provided few recommendations on alleviating poverty and increasing the standards of living through social programs. Most welfare policy recommendations were centered on cutting expenditures. For instance, the 2011 consultation with the Czech Republic found "rationalizing entitlements and the generous welfare system is unavoidable" (p. 11). Recommendations on unemployment benefits focused on reducing level and duration of benefits in order to strengthen job search incentives, reduce public expenditures and increase labor supply. The consultations rarely addressed poverty directly, though some consultations suggested that authorities better target programs to vulnerable populations as the expenditures are being reduced. The 2009 consultation with the Republic of Ireland found "it will be necessary to articulate a strategy that moves away from universalism in social welfare to one that

FIGURE 3
Country Frequency of Social Policy Recommendations for EU Countries, 2008-2011(in percent)

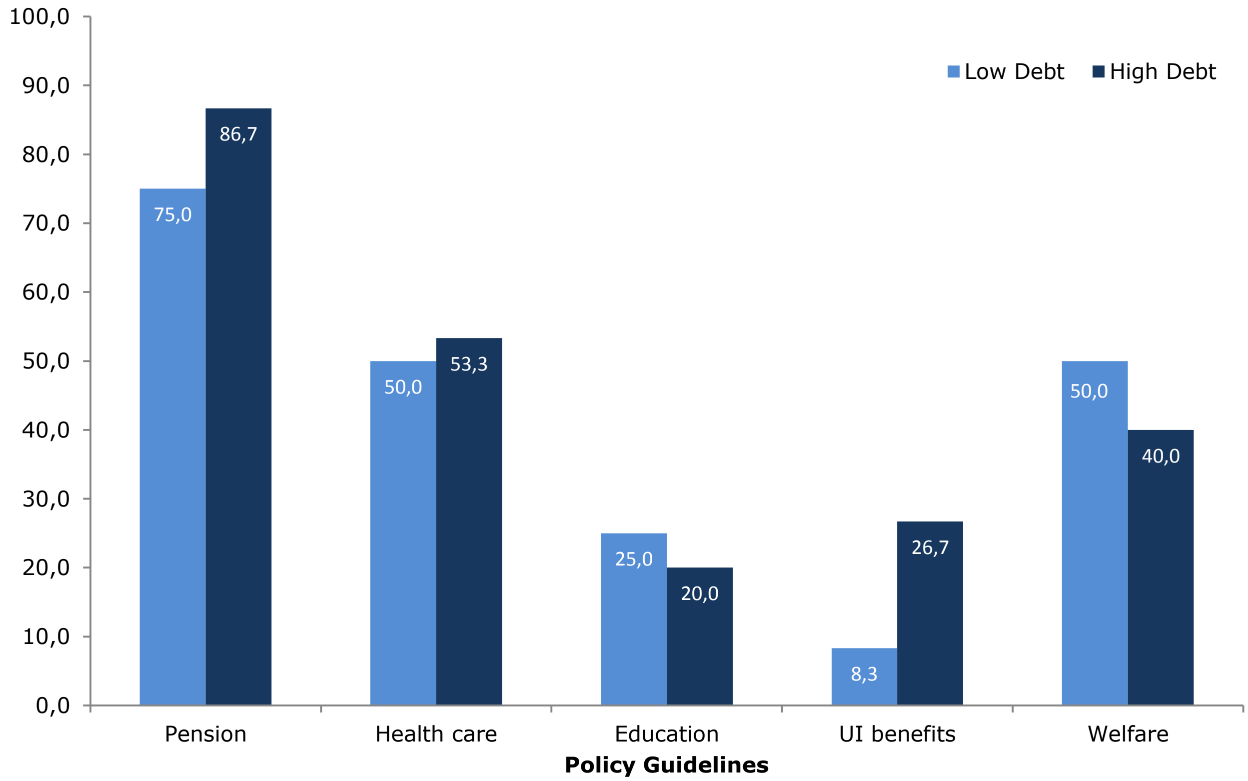


Source: Various Article IV consultation reports with EU countries, 2008-2011. Note: Education variable does not include advice on apprenticeship and training programs.

relies more on targeting and incentives" (p. 26). Though the Scandinavian countries out-performed many of the other EU countries on fiscal, employment and social measures during the study period, the IMF consultations did not make recommendations to expand the social welfare model.

Figure 4 summarizes the country frequency of IMF recommendations to reduce social program spending by level of debt. The 27 EU countries were divided into low and high debt countries. Twelve countries with an average gross debt below 50 percent of GDP (2008-2011) were categorized as low debt, and fifteen countries with an average gross debt of 50 percent or more were categorized as high debt. The country frequency rates for pension and unemployment benefit reductions were somewhat higher for high debt countries than for low debt countries. On the other hand, low debt countries received advice on reducing welfare spending at a higher frequency than high debt countries. However, it may be that policy measures with greater fiscal impact were recommended for high debt countries than low debt countries. The country frequency rates on reducing health care and education spending were nearly the same for the two groups of countries. Categorizing countries by projected gross debt in 2015 instead of average debt over the study period does not change these findings.

FIGURE 4
Country Frequency of Recommendations on Reduce Social Program Spending, by Gross Debt Level, for EU countries, 2008-2011 (in percent)



Source: IMF, World Economic Outlook Database, general government gross debt as percent of GDP, October 2012; and various Article IV consultation reports with EU countries, 2008-2011. Note: Average debt level over the period 2008-2011. Countries with average gross debt below 50 percent of GDP were categorized as low debt (12 countries), and countries with 50 percent or more were categorized as high debt countries (15 countries).

Europe 2020 and the IMF Article IV consultations

The Europe 2020 Strategy, adopted in 2010, outlines goals for "a smart, sustainable and inclusive economy" by 2020 (European Commission 2012a). The European Commission created five EU headline targets for employment, education, R&D, energy efficiency, and poverty. Each EU country has adopted their own national targets in each area reflecting different circumstances of the countries. The Europe 2020 Strategy is composed of seven flagship initiatives to reach these targets: 1) digital agenda; 2) innovation union to support R&D; 3) increase youth employment; 4) resource efficiency; 5) industrial policy for the globalization era; 6) agenda for new skills and jobs; 7) European platform against poverty.

The Europe 2020 Strategy provides few specifics on reaching the identified goals. For example, the concrete actions described for the Agenda for New Skills and Jobs are: improving flexibility and security (flexicurity), equipping people with the right skills, improving the quality of jobs and working conditions; and improving the conditions for job creation. However, EU president Barroso's speech (2012) about the Europe 2020 Strategy gave further insight into job creation policies and mentioned extending the retirement age, reforming labor markets and pension systems to make them more flexible, deregulation, opening up previously closed sectors, free trade agreements, and project bonds to increase investment in energy, transportation and digital infrastructure.

The lack of details on policies to reach the goals of the Europe 2020 Strategy makes it difficult to evaluate whether IMF Article IV recommendations are consistent or incompatible with the Europe 2020 strategy. There are several common themes for sustainable growth in the Article IV consultations and the Europe 2020 Strategy, including deregulation, open trade, and flexible labor markets. President Barroso observed that the Europe 2020 Strategy is a growth agenda that goes beyond fiscal consolidation, and it is therefore not necessarily inconsistent with the IMF 's fiscal recommendations. The Europe 2020 Strategy envisions a key role for public investment in energy efficiency, R&D and digital infrastructure for growth; whereas the IMF's focus of expenditure cuts as the center of consolidation leaves little room for public investment for a number of EU countries.

New skills and job creation are central to the Europe 2020 Strategy for sustainable growth and reduced social exclusion. One of the 2020 targets is to raise the average employment-to-population ratio to 75 percent for EU, with Denmark and the Netherlands having the most ambitious targets of 80 percent of 20-64 year olds being employed by 2020. Like the Europe 2020 Strategy, the IMF consultations focused on a combination of labor market flexibility and increased labor supply. However, the Europe 2020 Strategy couples increased flexibility with security (e.g. flexicurity), whereas the IMF consultations typically viewed security as a potential barrier for labor market entry. For example, the IMF consultations mentioned reducing duration and generosity of unemployment benefits as a mean to increase labor force participation.

Both the Europe 2020 Strategy and the IMF consultations see a role for vocational training and apprenticeship programs to increase employment prospects of young workers entering the work force and reduce job mismatches. Education is assigned a key role in the Europe 2020 Strategy to reach the growth goals, while the IMF Article IV consultations offered few recommendations on education. In the cases where recommendations on education were put forward, they were generally generic in substance such as "support investment in human capital," (Luxembourg 2011: p. 1) and "more widespread early childhood care and education" (Germany 2011: p. 11).

The biggest difference between the Europe 2020 Strategy and the IMF Article IV recommendations were in the areas of social policies. The IMF consultation primarily discusses pension and health care reform in the context of fiscal consolidation. Reducing the costs of an aging population was seen as the key to cutting public expenditures, and IMF recommendations focused on increasing the retirement age and reducing benefits. This differs from the Europe 2020 Strategy that lists improved access to social security and health care services. In terms of social policies to alleviate poverty, the IMF consultations promoted better targeting of benefits, which in the context of fiscal consolidation implied reducing benefits for most people, other than those with very low income, whereas the Europe 2020 Strategy promotes "better use of EU funds to support social inclusion" (European Commission 2012b).

Article IV consultation recommendations and the business cycle

The IMF Article IV consultations underestimated the severity of the recession in consultations with a number of countries. In the 2009 consultation with Greece, IMF staff predicted that "Greece's growth decline from peak to trough would still be milder than for the euro-area as a whole" (p. 11). Moreover, "staff projects some recovery in the late 2010" (p. 11). In fact, real GDP declined by 6.9 percent in 2011, and was projected to decline by an additional 6.0 percent in 2012 (IMF 2012a: Table A2). The 2008 consultation with Italy projected output "to contract by about ½ percent in 2008 and 1 percent in 2009" (p. 3). In 2009, Italy's real GDP declined by 5.5 percent, and the 2011 consultation report observed that "Italy suffered one of the largest output contractions in the euro area…and is experiencing one of the slowest recoveries" (p. 4).

In the 2007 consultation with France, "staff forecasts GDP growth of 1.6 percent in 2008, with a recovery in 2009" (p. 3). However, the 2009 report observed that "a severe recession hit France in 2008" with a real GDP decline of 3.1 percent in 2009. In some cases, the IMF forecasts were on target. For example, the 2008 consultation with Estonia predicted "a severe recession" for 2009, (p. 24) and advised Estonia authorities "to rein in the budget deficit despite the recession" (p. 22) In 2009, real GDP declined by 14.3 percent, and the 2009 consultation observed that "the economy is contracting sharply" (p. 5).

The unanticipated severity and duration of the economic downturn means that a number of IMF country consultations conducted in 2008 and 2009 did not modify advice to reflect actual economic circumstances. For instance, in the 2008 consultation with Denmark, the IMF staff argued that "the 2007 cyclical slowdown was welcome given record low unemployment and fast rising wages, but the global crisis has increased the risk of a hard landing" (p. 18). The consultation advised against an economic stimulus stating that "the case for further discretionary easing is weak because some slowing is needed to stop the decline in competitiveness" (p. 1). The next report for Denmark in 2010 began with observing that "Denmark is recovering from a deep recession," (p. 1) following a decline of 5.8 percent in real GDP in 2009.

Overall, there was no discernible change in medium and longer-term recommendations in the four policy areas of fiscal adjustment, inflation targeting, labor market policies and social policies identified in the content analysis. In some instances the framing of the advice shifted. For instance, in several earlier consultations concerns were expressed about labor supply shortages, while later-year consultations discussed increasing labor force participation. In some policy areas, recommendations became more specific over time. Reducing public spending related to aging of the population was a recurrent theme in the consultations. In earlier consultations, pension reform advice tended to be general and not specific to the country's specific circumstances, while later consultations provided more country-specific recommendations. For example, the 2008 consultation with Austria identified pensions as a "key area" for consolidation, but provided few specifics; whereas the 2010 consultation offered a list of recommendations ranging from "all other avenues to early inactivity for older workers… must also be closed rapidly" to "job opportunities for older workers need to be improved" (p. 9).

During the economic recession, a number of IMF consultations advised that automatic stabilizers be allowed to operate. However, in the cases of several countries, the IMF argued that there was not sufficient the fiscal space for counter-cyclical policy. The 2008 consultation with Estonia determined that there was "little room for countercyclical measures which would anyway be of only modest impact" (p. 3). Poland on the other had had let counter-cyclical measures fully operate, and the 2010 consultation determined that "the highly counter-cyclical fiscal policy has been a main reason for Poland's [economy] having avoided a recession" (p. 25).

Country Summaries

Austria

The 2008 Article IV consultation emphasized the need for structural reforms "with a special focus on further deregulation, increasing competition in domestic markets, and labor market reforms" (p. 1). The consultation provided few specific recommendations. Concerns about inflation hampering competitiveness were expressed and IMF staff encouraged opening up the energy and "free professions" markets for competition, as well as continued wage moderation (p. 17).

The 2009 Article IV consultation recommended "the development of a credible exit plan, aimed at structural fiscal consolidation over the medium term" (p. 1). IMF staff argued that "expenditure measures are preferable to tax hikes" (p. 32). "Key areas" identified for consolidation were "administration at lower levels of government, pensions, and education and health" (p. 32). The report also mentioned increases in fuel and property taxes as options (p. 21). Austria had recently implemented a medium-term budgeting framework but IMF staff cautioned "that the medium-term expenditures ceilings have to be sufficiently ambitious…for ensuring fiscal sustainability" (p. 21).

By 2010, the Austrian economy had recovered from the recession, and the 2011 Article IV consultation centered on "speeding up debt reduction by increasing expenditure efficiency." (p. 7) "Staff urged for stronger consolidation measures of at least ½ percent of GDP…until the structural deficit reaches zero" (p. 8). Three expenditures areas were identified for consolidation: pension, healthcare and subsidies (p. 9). Specific recommendations included, "the early retirement scheme for long-term insured should be fully abolished," "eligibility for disability pensions [should be] further reduced," and "all other avenues to early inactivity for older workers…must also be closed rapidly," while "job opportunities for older workers need to be improved" (p. 9). Furthermore, "the large efficiency gains that are possible in the health care sector should be promptly reaped" through centralized hospital planning, federal-level hospitals financing, and strengthening of outpatient treatment and prevention (p. 9). Finally, subsidies to public enterprises should be reduced (p. 9).

The consultation identified labor markets and education as two key areas for structural reform (p. 13). Labor market policies should focus on increasing labor force participation of older workers and low-skilled workers. Specific recommendations were "a reduction in social security contributions at the low end of the wage distribution," "measures to close the large educational attainment gap of children with immigrant background, "and "tertiary education reform to accelerate human capital accumulation" (p. 14, 16).

Belgium

The 2008 Article IV consultation stated that "the global financial crisis has hit the country particularly hard in recent months," (p. 3) and predicted that "Belgium will suffer a significant recession in 2009" (p. 4). In the near-term, IMF staff recommended "fiscal policy in 2009 should allow for full operation of the automatic stabilizers" (p. 4). But "once the current crisis is past, the fiscal stance will have to be significantly tightened to achieve long-run stability" (p. 4). Specific recommendations were "a structural adjustment of at least 0.7 percent of GDP per year once the crisis has past," and "returning the debt-to-GDP ratio onto a downward trajectory" (p. 21). To improve productivity and market efficiencies, IMF staff recommended "modifying indexation mechanisms within the current centralized bargaining framework," "easing of restrictions on new retail establishments, opening hours and sales periods," transparency in energy supply", making the "Competition Council… a watchdog against rent-seeking behavior," and deregulating prices and liberalizing the market for over-the-counter drugs" (p. 5, 18-19).

The 2009 Article IV consultation (released in March 2010) found "now that the worst of the recession seems to have passed, the time is ripe for ambitious action on the structural front" (p. 21). "Further labor market reforms are essential for increasing the labor supply and potential output." (p. 22) Specific labor market recommendations were to reduce rigidities stemming from labor taxes, "limit[] the level of unemployment benefits over time or their duration," "enhance monitoring of job search activities, apply penalties for refusals of suitable jobs, and increase job counseling and training opportunities" (p. 22). To increase labor market participation, recommendations focused on "raising the effective retirement age" and "extending activation programs to older workers," "reconsidering employment protection legislation," and "expanding job counseling and training opportunities" (p. 23). Post-crisis fiscal policy recommendations included, "adoption of a rule-based fiscal framework [to] help to increase the credibility of the consolidation efforts" (p. 4). IMF staff recommended "introducing a cap on total expenditure growth for each level of government and the social security administration while also considering additional revenue measures" (p. 20).

The 2010 Article IV recommendation reiterated the recommendations of the previous year. IMF staff agreed with the authorities' goal of a balanced budget (p. 4). "Achieving the appropriate objective of a balanced budget by 2015 will require…reform of fiscal federalism arrangements, spending constraints at all levels of government and social security, as well as revenue measures." (p. 1) To ensure credibility of consolidation, IMF staff advised "adopting a rule-based multiyear fiscal framework" (p. 1). Moreover, the IMF staff observed that "growth-enhancing structural reforms should be pursued vigorously" (p. 1). Labor market policies should focus on increasing labor market participation, wage flexibility, and reduce the tax wedge on wages (p. 28).

By 2012, "the outlook is clouded by slow growth across Europe. A recession in Belgium is already underway" (p. 36). In the intermediate-term, the 2011 Article IV consultation focused on "additional consolidation efforts [being] required to achieve structural balance by 2015" (p. 37). Where "additional consolidation effort should be centered on containing expenditures through entitlement reform and streamlining public sector employment, as well as on broadening the tax base" (p. 26). IMF staff advised that "measures should focus on the expenditure side, especially further pension reforms that would further raise the effective retirement age; measures to contain the growth rate of health care spending; and curtailing public sector employment" (p. 37). Finally, a burden-sharing agreement between different levels of government" that would impose spending caps was suggested (p. 27).

Bulgaria

With "one of the highest growth rates in Europe," IMF staff observed "Bulgaria's economy continued to perform well, helped by strong policies" in 2008" (p. 4). But "at the same time, external and internal balances widened further" (p. 4). The 2008 Article IV consultation recommended that "fiscal policies should aim at maintaining comfortable surpluses" (p. 4). The report stated that "a significant slowing of expenditures will also be necessary in later years" (p. 5). IMF staff expressed concerns about labor markets over-heating, resulting in deteriorating competitiveness (p. 4, 7). "Labor market overheated, with wage growth exceeding 20 percent, and annual inflation reached 12 percent" (p. 4). IMF staff argued that a "moderation in unit labor costs increases is essential" (p. 5). The consultation did not provide specifics on how to slow wage growth, and "the [Bulgarian] authorities reacted that the labor market was very flexible, and that wage growth would slow rapidly, when the economy slows"[9] (p. 36).

The economic "boom came to an end in the fourth quarter of 2008" when "a sharp adjustment in capital inflows led to a contraction of domestic demand… while recession in Bulgaria's trading partners caused a drop in exports" (2010: p. 4). The 2010 Article IV consultation discussed the need to shift growth from domestic demand to export (p. 13). For export-led growth to happen, "wage growth… will need to be moderate" (p. 14). The report noted that "authorities were confident that this [would] happen, arguing that the labor market was flexible" (p. 14). Moreover, containing wage growth in the public sector was seen to "help limit economy-wide wage growth and help competitiveness" (p. 19). IMF staff provided a number of recommendations for fiscal policies supportive to export-led growth: 1) urgent reforms of the social pension systems, including slowing pension benefit increases, increasing retirement age or minimum years of contribution, addressing underreporting of insurable income, and improve management of disability pensions; 2) comprehensive health care reforms to improve efficiency and quality, including rationalizing in-patient care; 3) rationalizing public administration and making it more efficient and effective; 4) containing public wage growth; and 5) a renewed push for privatization (p. 18-19). Education reform should focus on "improving quality of education, promoting life-long learning, and providing equal access to education" (p. 24). Finally "any tax rate reductions [such as lowering the social security contribution rates] would need to be compensated by further expenditure cuts" in the medium term (p. 17).

The 2011 Article IV consultation focused on "accelerating on-going reforms to regain growth potential, create jobs, and address aging-related pressures." (p. 1). IMF staff projected that a total adjustment of 2 percent of GDP between 2012 and 2014 would be needed to reach the medium-term fiscal objective of a 0.6 percent deficit (p. 13-14). IMF staff argued that "consolidation hinges on continued expenditure restraint," achieved through "tight spending ceilings, and "extension of the wage and pension bill freezes" (p. 14). staff also argued that "strong spending control should be accompanied by reforms" (p. 14). Recent health care reforms "should be complemented by steps to rationalize the hospital sector and improve information systems" (p. 14). Pension reform should include "further increases in the retirement age and service period, "change to a less generous indexation of benefits," "phas[ing] out of overly generous early retirement pensions," and "raising second pillar contribution rates" (p. 14-16). Finally, public administration reforms should be expanded to the municipal level and include workforce reduction and introduction of performance-

9 The unsustainable wage growth did slow subsequently, and in the 2011 report the IMF staff noted that "wage growth had moderated in the face of rising unemployment, and is now broadly in-line with productivity growth" (p. 10).

based remuneration without increasing the overall payroll envelope (p. 14). Education policies should address long-term youth unemployment "through active coordination of tertiary and vocational education with employers' needs (especially in tradeables sectors) and apprenticeships" (p. 10).

Cyprus

The 2009 Article IV consultation warned that "the steady deterioration in competitiveness threatens medium-term growth and viability" (p. 1). To increase competitiveness, IMF staff recommended structural reforms, such as eliminating or better targeting, "the inflation-indexed wage adjustment mechanism (COLA)," (p. 1, 24) and "the streamlining of red tape and bureaucracy, … supported by a bloated civil service" (p. 21). By 2009, "the global crisis ha[d] started to affect Cyprus. The overheating of the economy in 2007-08 ha[d] given rise to vulnerabilities." (p. 1) In order to meet the objective of medium-term budget balance and to avoid an unsustainable public debt-deficit cycle, "a ½- ¾ percent a year public consumption-based fiscal adjustment would be necessary." (p. 1) IMF staff argued that "a spending-based consolidation is appropriate as it would be more durable, given international experience" (p. 16). Specifically, "the reduction of the wage bill – a third of total spending – should be a key priority" (p. 17). "This would require hiring and wage controls and a more efficient use of civil servants" (p. 17). Flexicurity in the public sector and reducing lump sum payment to public retirees were also proposed (p. 23, 18). Moreover, further pension reform measures for all workers were suggested, such as raising the retirement age, and indexing benefits to prices (p. 18). "To further enhance social cohesion and protect the budget, social support measures should be targeted to reach the truly needy" (p. 17). Finally, "staff emphasized that it would be critical that the temporary stimulus measures be reversed when the economy recovers" (p. 17).

The 2011 Article IV consultation identified two key challenges: "to put in place a large and credible fiscal consolidation" and "ensure that banks and their supervisors are well-prepared to respond to possible adverse developments" (p. 1). A fiscal goal identified in the 2011 report was to bring the deficit below 3 percent of GDP by 2013 (p. 24). IMF staff and Cyprus authorities agreed on fiscal savings of 6.6 percent of GDP over 2011-13 (p. 18). Staff recommended that "additional measures need to be adopted… to balance the budget in 2014" (p. 19). "Measures should focus mostly on expenditure reductions, which" according to IMF staff "are more durable and reliable than revenue increases" (p. 24). Priority areas identified for consolidation were "containment of public sector wages and benefits and further improvements in the targeting of social transfers…, as well as a moderate increase in VAT rates" (p. 24). IMF staff also pushed for structural reforms to increase competitiveness. "The current crisis is an opportunity to undertake significant reform or even eliminate the cost of living adjustment system in the public sector" (p. 22). COLA reforms in the public sector were "expected to lead to reduced use of the COLA in the private sector" (p. 22-23).

Czech Republic

Following three years of rapid growth, the Czech economy was expected to slow sharply in 2009 (p. 3). In the 2008 Article IV consultation, IMF staff noted that "with low government debt and limited macroeconomic imbalances, there would be room for a discretionary fiscal stimulus under a more adverse scenario" (p. 4). But "over the medium term, the momentum of reforms will need to be restored to address long-term challenges and raise potential growth" (p. 4). The report mentioned improving work incentives through reforms of the labor market and the tax-benefit system, but did not provide specifics (p. 4). Monetary policy was viewed as being on the right track. "With inflation likely to fall below the CNB's target of 3 percent…, scope exists for further easing" (p. 17). IMF staff agreed with the new inflation target of 2 percent in 2010, noting it aligns with the ECB's inflation target, and would help the Czech Republic meet the Maastricht criteria for euro adoption (p. 19).

The 2010 Article IV consultation focused on "the urgency of fiscal adjustment" highlighted by the crisis (p. 4). The report states: "During the years of rapid economic growth the opportunity for more fundamental fiscal consolidation was missed" (p. 4). Moving forward, "fiscal consolidation… should focus on both expenditure and revenue measures." But IMF staff noted "international experience suggests that expenditure-based fiscal consolidations tend to be more durable" (p. 5). Specific recommended expenditure measures were: "reorganizing public institutions and positions would help reduce the overall wage bill;" "introducing means-testing for social benefits," and "improve efficiency of public services." Revenue measures included "eliminating tax exemptions and loopholes" (p. 5). IMF staff stressed that "rationalizing mandatory expenditures and the generous welfare system is unavoidable" (p. 5). The staff recommended pension reforms that would "better link contributions to benefits and further increas[e] the effective retirement age;" "a tightening of the criteria for disability pensions," and "moving to a fully funded second-pillar private pension scheme" (p. 5, 33). The staff found that "fundamental health care reforms are equally important" (p. 5) and recommended "reduc[ing] the broad coverage of publicly provided and insured services and allow greater scope for private sector provision of health services;" and introduc[ing] voluntary insurance, personal health accounts, and choices in health benefits plans to ensure long-term financial sustainability of the health care system" (p. 6).

The staff predicted that "the adverse effects of the crisis are likely to be long lasting," and argued that "swift implementation of growth-enhancing structural reforms becomes critical" (p. 6). Specifically, "promoting work incentives through changes to the tax-benefit system, improving labor market flexibility and the quality of education, and further reducing barriers to business entry and exit" (p. 6). Finally, a shift in monetary policy was recommended. "The easing cycle of monetary policy seems to have come to an end. The supportive monetary policy stance… should shift to tightening as the recovery gathers momentum" (p. 4).

By 2011, IMF staff noted that "the Czech economy ha[d] rebounded from the downturn owing to its strong fundamentals and the global recovery, but faces a number of policy challenges" (p. 18). Therefore, the IMF argued that "wide-ranging structural reforms are needed to buttress growth" (p. 19). Specific structural reforms should focus on "increasing labor participation and labor market flexibility; enhancing efficiency in higher education, R&D, and the public sector; and further improving the business climate" (p. 19). Moreover, "staff urged the authorities to identify and put in place a credible package of medium-term consolidation measures… In staff's view, rationalizing entitlements and the generous welfare state is unavoidable to ensure durability of fiscal adjustment" (p. 11). The consultation report reiterated the consolidation measures proposed in the previous consultation. In terms of monetary policy, IMF staff recommended "maintaining accommodative monetary policy until the negative output gap narrows" (p. 1). but warned "a rise in inflation expectations or a rapid improvement in labor markets would warrant earlier action" (p. 19).

Denmark

The 2008 Article IV consultation mostly praised Denmark for its economic policies, using language such as "steady hand on fiscal policy," "responses to the financial crisis were innovative, forceful, and timely," "agreed increase [in financial sector surveillance] is welcome," "generous provision of foreign aid is welcome," and "the proposed 2009 budget strikes a good balance between allowing growth to slow and cushioning it from a severe recession" (p. 18-9). The consultation provides three specific recommendations: 1) "upfront action is needed to ensure fiscal sustainability" to close the long-term fiscal gap; 2) "tax reform needs to be more comprehensive" and 3) user fees, indexation of the tax on residential property and reducing the deductibility of mortgage interest should be considered (p. 18-19).

The report noted that "the 2007 cyclical slowdown was welcome given record low unemployment and fast rising wages, but the global crisis has increased the risk of a hard landing" (p. 18). The main concern of the consultation was that recent trends relating to competitiveness were unsustainable. "Wage growth needs to slow if firms are to rebuild profitability and stem the decline in Denmark's export share" (p. 18). Due to concern about competitiveness, IMF staff stated that "the case for further discretionary easing is weak because some slowing is needed to stop the decline in competitiveness" (p. 1).

In the 2010 Article IV consultation, the emphasis on recommendations had changed to the longer term. The report begins with stating that "Denmark is recovering from a deep recession" (p. 1). Nonetheless, the main labor market recommendations related to addressing the "looming labor supply pressures" (p. 26). IMF staff recommended "phasing out early retirement schemes and reforming sickness and disability leave benefits" in order to increase labor supply (p. 26). Furthermore, staff recommended increasing labor productivity growth by "reforms that intensify competition and accelerate firm exit and entry;" as well as, "measures that increase the return to education, at higher skill levels in particular" (p. 26). Fiscal policy recommendations focused on "embark[ing] on a multi-year consolidation program;" "bringing down the deficit to below the Stability and Growth Pact's ceiling;" and "reducing public consumption growth" (p. 30). Finally, the report noted that "the peg to the euro continues to service Denmark well," but recommends eventual adoption of the euro (p. 29).

Estonia

The 2008 Article IV consultation report predicted a "severe recession" for 2009 (p. 24). The key fiscal challenges, identified by IMF staff, were "to rein in the budget deficit despite the recession and restore a sustainable fiscal stance over the medium term" (p. 22). Moreover, IMF staff observed that "large expenditure increases over the past two years [were] unsustainable and [left] little room for countercyclical measures which would anyway be of only modest impact" (p. 3). Market flexibility was seen as "critical for the restructuring needed to support medium-term convergence" by IMF staff (p. 24). The staff supported legislation to increase labor market flexibility, but "advised that the fiscal costs of social protection be clearly assessed and accounted for, and expressed concern about possible adverse labor supply effects" of strengthening social protection by increasing unemployment benefits (p. 24).

By early 2010, "the economy [was] contracting sharply," and unemployment was projected to reach 16 percent (p. 5). Fiscal policies in the 2009 Article IV consultation focused on meeting the Maastricht criteria for euro adoption in 2011. IMF staff argued that "the benefits of euro adoption outweigh the mildly procyclical effects of fiscal tightening during the crisis" (p. 3). The staff predicted that the "euro adoption by itself is unlikely to trigger any major change in the pace of recovery," and recommended that "the focus… be on restoring economic stability and laying the foundations for more balanced growth" (p. 3). Much of the adjustment would come from the revenue side, since "the need to protect social safety nets limits the room for spending cuts" (p. 4). Specific tax measures mentioned were to eliminate "poorly targeted exemptions," review corporate income tax deferral rules, and enhance use of environmental and property taxes," and "increase the VAT rate" (p. 4).

On January 1, 2011, Estonia joined the euro area. The 2010 Article IV consultation report released in January 2011 noted that "Estonia has the distinction of being the only EU country, aside from Sweden, whose fiscal deficit does not exceed the Maastricht limit" (p. 1). The staff attributed Estonia's success with "authorities' policies hav[ing] largely been in line with Fund Advice" (p. 9). Looking forward, IMF staff agreed with "authorities' medium-term goal of restoring a balanced budget" (p. 1). "This will imply reducing expenditures by about 3 percent of GDP and thus bringing Estonia's public spending closer to its pre-crisis level" (p. 10). With an unemployment rate estimated at 17.6 percent in 2010, IMF staff recommended "addressing skill mismatches through continued progress in enhancing the education system" (p. 16; Table 1). EU-structural funds were envisioned as a source for funding. "EU structural funds can continue supporting life-long learning, increases in labor mobility, and needed infrastructure investment" (p. 1).

The 2011 Article IV consultation emphasized sustainable growth. This would "entail enhancing Estonia's attractiveness for FDI, addressing skill mismatches, and increasing human capital" (p. 18). The report noted that "overall unemployment, while declining, remains high with long-term joblessness on the rise" (p. 4). Moreover, "long-term unemployment has continued rising reflecting jobs-skills mismatch" (p. 5). The consultation identified "emerging labor market tensions" of labor shortages and increases in manufacturing job vacancies, despite double-digit unemployment (p. 16). IMF staff agreed with the authorities approach of reducing skill mismatches through vocational education and training programs and a new one-stop IT platform. (p. 16) Furthermore, staff recommended foster[ing] development of human resources in technical fields as well as to attract highly-trained individual from abroad" (p. 17).

Finland

The 2008 Article IV consultation stressed long-term fiscal sustainability. "Containment of government spending is a priority" due to aging of the population (p. 13). IMF staff stated that "a permanent improvement in the structural primary balance after 2011 of at least 1½ percent of GDP is needed to stabilize net public debt" (p. 19). Where "the bulk of the needed adjustment should rely on containment of spending" and improved efficiency in the government sector (p. 19). To contain demand for public services and increase competition in their provision, IMF staff recommended "increase[ing] recourse to user charges for public services" and "contracting out, outsourcing, and well-designed public-private partnerships" in care for the elderly and children (p. 14). To address tight labor markets, IMF staff recommended structural reforms in the form of "labor-income tax cuts that promote labor force participation" (p. 19). However, staff advised against the planned cut in the VAT rate on food (p. 19). Other recommendations mentioned, but not discussed in detail, were "steps to strengthen activation of the unemployed and partially disabled, shorten time spent in tertiary education, improve training and reduce labor market mismatches, and lessen poverty traps" (p. 20).

The 2008 consultation report stated that Finland was among the best EU performers, but noted the economy faced important challenges (2008: p. 1). In 2009, the economy was "amid a massive economic downturn," (2010: p. 21) with GDP falling almost 8 percent in 2009 (p. 1), and the 2010 Article IV consultation report observed that "Finland ha[d] been dealt a severe blow by the global crisis"[10] (p. 1). Therefore, IMF staff recommended against "ambitious fiscal tightening in 2011," and "advised a more measured pace of consolidation" (p. 1). Beyond 2011, staff recommended "an adjustment of about ½ percent of GDP per annum" to close the sustainability gap by 2020 (p. 28). The staff wrote: "international evidence generally indicat[es] that expenditure-based consolidations have been more successful" (p. 26). Specific expenditure retrenchment measures mentioned were "increase in effective retirement age and measures to restrain growth in demand for health- and long-term care," "higher tuition fees and a reduction of student grants in favor of loans for tertiary education," and "creating incentives for reducing time to graduation" (p. 26).

France

The 2007 consultation report forecasted "GDP growth of 1.6 percent in 2008, with a recovery in 2009" (p. 1). However, the 2009 Article IV consultation report observed that "a severe recession hit France in 2008" and forecasted "real GDP to contract by 3 percent" in 2009 (p. 5). Most of the consultation assessed the economic status of the French economy, and discussed fiscal consolidation and labor market reform. IMF staff stated that "historical experience indicates that successful fiscal consolidations were often launched in the midst of economic downturns or the early stages of recovery" (p. 20, no references were provided). Therefore, IMF staff recommended a "decisive implementation of a clear consolidation strategy at all levels of government [to] be anchored in the 2010 budget" (p. 20). Longer-term reforms should "strengthen financial stability, safeguard fiscal sustainability and deepen the reform of labor and product markets" (p. 3). Labor market recommendations centered on labor market activation and training policies, minimum wage moderation, and raising the legal retirement age (p. 4).

The 2010 Article IV consultation "focused on the need for credible consolidation to safeguard fiscal sustainability without endangering the fragile recovery" (p. 1). Introducing multi-year budgetary frameworks and a fiscal rule on the structural government balance with built-in debt-brake mechanism would strengthen the credibility of consolidation (p. 19). IMF staff wrote that "entitlement reforms in the pension and health care systems are key" for credible fiscal consolidation (p. 30). In order to increase growth, IMF staff also recommended "policies to encourage wage moderation, foster research and development, promote innovation, improve competition, and create favorable conditions for businesses to grow" (p. 24). In order to avoid a rise in structural unemployment, "staff suggested to consider temporary hiring incentives (in the form of credits for new hires or lower payroll contributions)," a unified job placement agency, improved training opportunities, and strict enforcement of job-search requirements (p. 26). The report further

10 Finland, real GDP declined by 8.5 percent in 2009, according to IMF World Economic Outlook, Table A2.

noted that "introducing greater competition in health-related services and professional services… would be welcome" (p. 29).

In the 2011 Article IV consultation, the focus was on reducing the debt: "Achieving the fiscal targets and further entitlement reform are important to lower the public debt to 60 percent of GDP by the middle of the next decade" (p. 38). IMF staff argued that "securing long-term fiscal sustainability will require deeper reforms of key pension and health care parameters" (p. 21). Pension and health care reform recommendations concentrated on further increasing the legal retirement age, targeted tax incentives to increase senior workers' labor force participation, continued efficiency gains in health and long-term care, and tighter budget constraint on spending by social security entities (p. 16, 21). To attain fiscal sustainability, IMF staff encouraged the adoption of a fiscal rule that would include multi-year expenditure ceilings, minimum annual revenue measures, and restriction of new tax measures (p. 19). Tax reform recommendations were reducing the high labor-tax wedges, make earned income tax credits more generous for older workers and women with school-aged children, and lowering the statutory rate of corporate taxes (p. 34-5). Moreover, gradual elimination of VAT exemptions and incentives, introduction of a carbon tax, higher revenue from fuel, alcohol and tobacco taxation, and hikes in recurrent property taxes were also mentioned (p. 17). The section on labor market reform reiterated most of the recommendations from the 2010 consultation, but added easing employment protection and reducing the duration or level of unemployment benefits, and phasing out pre-retirement benefits to the list of reforms (p. 35-6).

Germany

The 2008 Article IV consultation report predicted that "Germany faces the prospect of a sizeable, and possible extended, economic downturn" (p. 1). IMF "staff argued for a more ambitious stimulus now" (p. 1). To ensure long-term public finances sustainability, the staff recommended recommitment of a fiscal rule that "limits the structural budget balance to close to zero" at federal and state level (p. 27). One identified risk to fiscal sustainability was health care costs due to the aging of the population, and further cost savings measures were proposed, including rationalization in pharmaceutical expenditures and efficiency-enhancing competition (p. 28, 31).

In the 2010 Article IV consultation, German authorities stated they "are firmly committed to meeting their medium-term fiscal targets" (p. 18). IMF analysis found that in order to achieve these, annual structural adjustment of ½ percent of GDP in 2011-13 and ¾ percent of GDP through 2016 would be required (p. 18-9). IMF staff argued that "expenditure-based consolidations tend to be larger and more enduring," (p. 19) and proposed a fiscal adjustment strategy which focused on expenditures, including "examination of subsidies," strict adherence to agreed-upon "adjustment mechanisms for pension benefits and the gradual rise in the retirement age," and "limiting spending on non-generic pharmaceuticals" (p. 19). Increasing "contribution rates to the unemployment insurance" was also mentioned (p. 19) Moreover, "should revenue measures have to be part of the solution, eliminating exemptions in income and VAT taxes should have priority" (p. 32). Labor market reform recommendations focused on "increasing labor market flexibility through decreasing both legal and labor-court based employment protection" (p. 27).

In the 2011 Article IV consultation, IMF staff viewed "the proposed consolidation path as appropriate" (p. 25). But they cautioned that the "pace of consolidation be slowed in case of a substantial negative shock to growth" (p. 25). To rebalance public finances in the longer term, IMF staff recommended increasing labor force participation by introducing "in-work credit programs for the elderly and secondary earners," "an earned income tax credit for low-income," and "tax reform that would move to individual taxation of married couples" (p. 27). IMF staff stated that "corporate taxes are the most harmful [among all taxes] to economic growth," and proposed "abolishing the local level trade tax (p. 28). The recommended tax cuts would be paid by "eliminating concessions in VAT and raising property and inheritance taxes" (p. 28). On the expenditure side, "elimination of the unconditional child transfers" and other unspecified social entitlements were mentioned (p. 28). The consultation also advocated for educational reform and physical investment and innovations (p. 39). The staff agreed with German authorities that there is a need for "more widespread early childhood care and education," as well as "reorienting vocational training" (p. 11).

Greece

In the 2009 Article IV consultation report, IMF staff predicted that "Greece's growth decline from peak to trough would still be milder than for the euro-area as a whole…Staff project[ed] some recovery in the late 2010" (p. 11). IMF staff warned that "fiscal consolidation cannot be postponed;" (p. 34) and argued for a "coherent sustained fiscal adjustment plan" and recommended "annual adjustment of about 1½ percent of GDP in permanent measures beginning in 2010 to place public debt on a declining path" (p. 23). On the revenue side, IMF staff recommended "focus[ing] on income that escapes taxation… by phasing out exemptions and deductions; taxing the self-employed and the informal sector; and increasing further selected excise taxes" (p. 24). On the spending side, "wage moderation (extended to pensions) and restrictive hiring policies" were proposed "to curb the fast growing wage bill" (p. 24). Moreover, "Greece urgently needs further pension reform" and "staff noted that parametric reforms remain essential to ensure that pensions of next generations can be paid and should not be postponed" (p. 26). Addressing unemployment, IMF staff wrote: "more government spending cannot be used as a substitute for labor reforms" (p. 30). Specific labor market reforms mentioned were to "promote a social contract focused on employment growth through strong wage moderation;" expand part-time work opportunities;" and "reduce employment protection" (p. 33). The IMF did not conduct Article IV consultation with Greece in 2010 and 2011.

Hungary

The 2008 Article IV consultation emphasized fiscal consolidation to put the government debt-to-GDP ratio on a downward path and inflation targeting (p. 5). "Monetary policy should aim to reduce CPI inflation to the 3 percent target over two years" (p. 3). The report stated that "further consolidation [would be] required" (p. 12). "Staff supported the introduction of a rules-based fiscal framework" (p. 15). Moreover, "to boost potential GDP growth, a smaller size of government… would help" (p. 3). To reduce the ratio of government spending to GDP, "further reforms of the pension, health, and education sectors are necessary" (p. 16). Specific recommendations were "further increase in the effective retirement age," "improve the governance of hospitals and increase efficiency by adopting a sound regulatory framework" in health care, "expanded performance-based financing and greater autonomy of higher education institutions," and better targeting of social transfers by "increasing means testing and tightening eligibility criteria" (p. 16).

In the 2010 Article IV consultation, "staff advocated to focus on expenditure rationalization and structural reforms." (p. 1) "A credible medium-term fiscal adjustment program to safeguard fiscal sustainability could set off a virtuous cycle of lower risk spreads, reduced public and private financing costs, and, ultimately, higher growth" (p. 1). Areas identified for consolidation included "poorly targeted social benefits and price subsidies" (p. 17).

The 2011 Article IV consultation noted that "Hungary has yet to recover from the previous crisis but is now facing renewed pressure" (p. 15). But "despite the weaker growth outlook," IMF staff argued that "the planned fiscal tightening is necessary" (p. 16). Moreover, "the constitutional mandate to maintain public debt below 50 percent is commendable" (p. 16). "Staff expressed concerns about the underlying composition of fiscal policy" (p. 8). To "minimize adverse effects on medium-term growth prospects and the poor," IMF staff proposed "eliminating special sector levies, revisiting elements of the flat tax, and rationalizing related wage and compensation reforms" (p. 8). "Staff also raised broader concerns about long-term growth," and "emphasized obstacles regarding investment and labor participation as particularly worrisome" (p. 14). In terms of monetary policy, "the MNB's tightening bias is justified" (p. 1).

Ireland

By 2009, "the Irish economy [was] in the midst of an unprecedented economic correction" (p. 28). The 2009 Article IV consultation report stated that "fiscal consolidation has begun – and requires a sustained effort" (p. 1). Fiscal consolidation focused on expenditure measures. IMF staff argued that "the international evidence is clear: fiscal adjustment should focus on expenditure cuts" (p. 26). Fiscal recommendations included "the public wage bill and the scope of social welfare programs" (p. 26). Staff wrote: "social welfare expenditures must better target the vulnerable," (p. 26) and "the authorities recognized that it will be necessary to articulate a strategy that moves away from universalism in social welfare to one that relies more on targeting and incentives" (p. 26). Proposals included "earned income tax credits," "indexing of benefits to more appropriate price baskets," "more nuanced minimum wage structure," and "reduce social transfers" (p. 26). A recently adopted wage freeze and pension levy reduced the effective wage by 7.5 percent in the public sector, and the staff recommended that "further ratcheting down of the public pay structure and employment levels" was needed for sustainable fiscal consolidation (p. 26, 29). On the revenue side, IMF staff recommended "limiting tax relief on mortgage interest," "raising social security contributions," as well as the possibility of introducing a property tax (p. 27).

The IMF staff supported the Irish authorities' response to the economic crisis in the 2010 Article IV consultation. "Staff supports the appropriately ambitious fiscal consolidation plan through 2014 but cautioned that the required adjustment may be larger than projected" (p. 24). IMF staff observed that "this is also a good moment to establish a strong fiscal framework. A medium-term fiscal framework incorporating expenditure ceilings is a valuable management tool" (p. 27). However, the 2010 consultation provided few specific recommendations for further consolidation. Staff and authorities agreed that expenditures saving will remain central to achieving consolidation, and "entitlement reforms could generate further savings" (p. 25).

Italy

In the 2008 Article IV consultation, IMF staff argued for the budgeted fiscal consolidation being delayed. "The target deficit of 2.1 percent of GDP for 2009 is no longer in line with the deteriorating macroeconomic environment" (p. 3). Still staff emphasized that "the current crisis should not eclipse the need for bolder action to address longer-term fiscal challenges." (p. 25) Specifically, further reforms to the welfare system, including "future increases in the retirement age (especially for women)" (p. 25). IMF staff also recommended structural reform in the labor market, retail trade and services and the energy market. Labor market reform "broadening and streamlining the social safety net, in particular the unemployment benefit system," financed by "reducing replacement rates and spending on active labor market policies, and by eliminating…tax reductions on overtime/bonus pay" (p. 31). Finally, reductions in labor taxation should be "combined with modification of the wage bargaining framework that increase the scope for firm-level bargaining" (p. 31).

By 2010, "the recovery [was] expected to be modest" (p. 11). Moreover, "the staff's medium-term scenario is less optimistic than the authorities" (p. 16). In the 2010 Article IV consultation, IMF staff argued that "the planned consolidation is not ambitious enough," and "would still not deliver the medium-term objective (MTO) of structural balance" (p. 16). Medium-term fiscal consolidation "should be based on rationalizing current spending" (p. 22). IMF staff endorsed the authorities' plan but warned that "consolidation should also include strict adherence to budget targets" (p. 22). In order to bring the debt-to-GDP ratio to 60 percent, "additional savings from age-related expenditures (equivalent to cutting nominal pensions by 5 percent over the long term) would still be needed" (p. 21). Further pension reform should include "revisiting the current high replacement rates and increasing the age of retirement age" (p. 21). IMF staff reemphasized the need for "a second generation of labor market reforms" (p. 27, 30). They proposed that "the public sector should take the lead in decentralizing wage bargaining arrangements" to take regional differences between the north and the south into account (p. 27).

The 2008 consultation report projected output "to contract by about ½ percent in 2008 and 1 percent in 2009" (p. 3). In fact, real GDP declined by 5.2 percent in 2009. The 2010 consultation report noted that "although the worst effects of the global financial crisis on Italy's economy have mostly passed, key vulnerabilities remain" (p. 29). The 2011 consultation noted that "Italy suffered one of the largest output contractions in the euro area…and is experiencing one of the slowest recoveries" (p. 4). In the 2011 Article IV consultation, IMF staff stated that "fiscal consolidation is a prerequisite for sustainable growth…but only sustained growth will reduce the burden of public debt" (p. 1). Fiscal consolidation "should be achieved by rationalizing public expenditure and reducing tax evasion," (p. 1).Staff predicted "containing public sector wages could generate positive spillovers for the private sector" (p. 30). The staff also recommended acceleration of pension reform, including increasing women's retirement age from 60 to 65 years (p. 20, 23). To increase potential growth "comprehensive structural reforms in the areas of labor and product markets and public administration should be promptly implemented" (p. 1). Staff acknowledged that "the partial liberalization in the labor market may have undermined investment in human capital and innovation," (p. 27) and recommended "harmonizing labor contracts and legislation between protected and unprotected workers" (p. 27). Specifically, "a more decentralized wage bargaining system" (p. 27). In the 2011 report, the staff also noted that Italy's "educational attainment and quality of education are among the lowest across OECD countries" (p. 28). The report did not offer any specific recommendations on education, other than noting that better education should be ensured in the South (p. 26). Finally, the staff noted "combating organized crime, corruption, and related money laundering, should remain a priority" (p. 31).

Latvia

The IMF conducted one Article IV consultation (in 2010) with Latvia in the study period. Latvia had experienced a severe economic downturn with "an 18 percent contraction in 2009 and substantial volatility" (p. 4). The 2010 consultation focused on "restoring growth and reducing unemployment," "completing the fiscal adjustment to meet the Maastricht criteria," "resolving the private sector debt overhang," and "structural reforms to improve competitiveness and raise potential growth" (p. 23). Reducing unemployment was mentioned as a means to increase growth: "Reducing unemployment further, to around 10 percent, could raise growth by an additional 2-3 percent" (p. 23). IMF staff recommended structural reforms to reduce unemployment, "given constraints to expansionary macroeconomic policy" (p. 25). Specific reforms discussed in the consultation were: 1) "minimum wage cuts [to be] combined with labor tax cuts for the low-paid;" 2) "in the short run, increasing domestic demand"… through debt restructuring and strengthening of the financial system; and 3) in the longer term, "improving educational performance" (p. 25). IMF staff warned that "there is a risk that hysteresis effects could raise the natural rate and make higher unemployment permanent" (p. 25).

The staff emphasized the need for completing the fiscal adjustment, while acknowledging difficulties in attaining goals of debt sustainability. For instance, "the government's pension cut [of 70 percent for working pensioners] was ruled unconstitutional for violating pensioners' legitimate expectations" (p. 28). "Staff estimate[d] a further 6 percent of GDP in adjustment remains necessary," to meet the Maastricht deficit criteria by 2012 (p. 29). The staff argued that "while continued adjustment might worsen the recession, delaying it would…. undermin[e] the euro adoption strategy" (p 29). Current expenditure cuts were preferred as "international experience suggests [they] generate more sustainable adjustment" (p. 29) "But revenue measures may also be required" (p. 39). Current expenditure cuts identified were pensions, subsidies and transfers. "Staff noted large past increases in pensions as well as subsidies and transfers, and welcomed efforts to reexamine the budget for additional savings" (p. 39).

Lithuania

In 2009, "the Lithuanian economy [was] undergoing a painful adjustment" (p. 3). In the 2009 Article IV consultation, "staff advocated a sizeable fiscal consolidation to ensure that public debt is sustainable" (p. 1). Where, "fiscal consolidation should be guided by the need to… sustainably bring spending to more affordable levels, primarily through savings in social benefits and public sector wage bill," "broaden the tax base," "strengthen fiscal institutions," and "protect the most vulnerable including through rationalization of generous benefits" (p. 3). The staff noted that "the scope for savings appear to be greatest in social benefits and civil service pay" (p. 14). They also recommended "to bring [pension] benefits in line with contributions and restore full funding of the second pension pillar,… gradually increase retirement age,… tighten eligibility for child, disability and sickness benefits, and decrease the term of maternity benefits to international levels" (p.14). The staff also found there was "scope for savings in the education sector… with a very low student-teacher ratio." (p. 14). Along with spending cuts, the staff advised "it would also be prudent to raise the tax-to-GDP ratio" (p. 14). IMF staff acknowledged that "in the context of such a large scale economic adjustment, it will be important… to provide space for social safety nets" (p. 15).

The 2011 Article IV consultation discussed how to enhance prospects for euro adoption in 2014 (p. 1, 14). IMF staff made the case for "additional fiscal consolidation [to] secure sound public finances;" (p. 14) and estimated that "some 5½ percent of GDP in additional measures… [were] required" (p. 15). Specific recommendations included reform of the social security system, increasing tax revenues, such as introducing a real estate tax on personal property and an annual car tax, and structural reforms in the education and health sectors (p. 17-18). Specifically, "reform of the social security system should be assigned the highest priority," and recommendations included "limiting the duration of [parental] benefits, introduce a benefit cap… [and] tighter certification of sickness and disability" (p. 17). Pension reform recommendations were similar to those of 2009. Furthermore, IMF staff proposed "consolidation within the dense hospital network and a greater reliance on primary care, out-patient services, and patient copayments" (p. 18). The unemployment rate was projected to rise to 18 percent in 2010, (Table 1) and staff observed that "the high level of unemployment calls for decisive policy action" (p. 27). The staff found that "proposals in parliament to expand fixed-term contracts, ease dismissal requirements and allow greater flexibility in overtime [would] further increase labor market flexibility and encourage firms to hire" (p. 27).

Luxembourg

"Luxembourg face[d] its most severe recession since… the 1970s," (p. 1) and the 2009 Article IV consultation recommended "automatic stabilizers [be] allowed to function fully" (p. 19). However, "over the medium and long term adjustment is necessary to foster fiscal sustainability" (p. 18). Specific recommendations were reconsideration of "full inflation indexation of wages and benefits," "address aging-related challenges," and "far-reaching reforms of the public pay-as-you-go pension system" (p. 1, 20).

To support medium-term fiscal adjustment, the recommendations in the 2010 Article IV consultation focused on establishing "a medium-term fiscal framework that, supported by medium-term targets and binding multi-year expenditures, would … safeguard fiscal sustainability" (p. 16). In the medium term, "ensuring fiscal stability requires…substantive pension reform" (p. 4). Specific reform measures mentioned were "gradually increasing the effective and statutory retirement age," discourage early retirement, and "improving the alignment of benefits and contributions" (p. 16).

In the 2011 Article IV consultation, IMF staff expressed concern that fiscal consolidation comes from cap on public investment. "In the medium term, this cap should be replaced with current spending cuts – notably by rationalizing social transfers and subsides" and "curtailing other current spending, including increases in the public sector wage bill" (p. 1, 12, 17). The staff reiterated their recommendations on pension reform to increase the effective retirement age and "limiting pension benefit indexation" (p. 14). The staff also urged moving up the schedule for the implementation of approved health care reforms (p. 1, 14). To boost Luxembourg's competitiveness, IMF staff recommended "revamping the system of social transfers and subsidies," address mismatched skills, and support investment in human capital" (p. 1). Efforts to curtail wage growth included "a need in the short run to curb automatic wage increases," while in the longer term authorities were advised to eliminate wage indexation (p. 1, 17).

Malta

Because of "Malta's high vulnerability as a small and very open economy," IMF staff recommended "particularly prudent debt management" in the 2010 Article IV consultation (p. 9, 18). The emphasis of the consultation was on "growth friendly and ambitious fiscal consolidation and… establishing high value export activities" (p. 1). IMF staff agreed with the Malta authorities' goal of reducing the deficit to 1.4 percent of GDP by 2013, but warned that the deficit target may not be met based on staff's "conservative growth outlook" (p. 18). IMF staff made the case for additional cost-saving measures coming from the expenditure side "through personnel retrenchment" and reducing "age-related public spending" (p. 10). "Additional changes to the current PAYG [pay-as-you-go] system could include indexing the retirement age to life expectancy, or further lengthening the contribution period for full entitlement" (p. 12). Moreover, staff mentioned "a timely but gradual introduction of an additional mandatory and privately funded pillar" (p. 12). The consultation also discussed proposals to boost labor utilization and productivity by introducing "more flexible arrangements for part-time work and flexible working practices," and "linking wage increases to productivity gains." To "help satisfy the demand for higher skills," staff recommended "increasing human capital through better targeted support, aimed at retaining the highly qualified, as well as improving primary and secondary education" (p. 7). "Support for higher education should continue,… but accompanied by rigorous means testing" (p. 7).

Netherlands

In the 2008 article IV consultation report, IMF staff predicted that "with a tightening labor market, wages are anticipated to accelerate" (p. 1). "Efforts to increase employment are crucial to ease growing labor shortages, support growth, and address the impact of population aging" (p. 25). Therefore, "reforms of the tax system, social entitlements, and employment protection, supported by enhanced activation strategies, are needed to stimulate employment" (p. 25). Specific recommendations included: reducing the high effective marginal tax rates on second family earners to promote female employment, targeted tax incentives to induce elderly participation, stricter enforcement of work availability requirements, tightening reassessment of disability status, liberalization of strict employment protection legislation (EPL) for regular employment, and introduction of a funded severance pay system to enhance labor mobility (p. 25). To promote productivity, the staff recommended removing barriers to entrepreneurship through liberalization of zoning regulations and rigid shop opening hours (p. 25). To alleviate mounting labor market pressures from output being above potential, the staff recommended "some withdrawal of fiscal impulse" (p. 1).

In the longer term, "fiscal sustainability requires a robust surplus permanently higher… around 3 percent of GDP in 2011" (p. 13). Where "adjustment should focus on expenditure retrenchment or tax base broadening" (p. 1). Due to rising expenditures from an aging population, IMF staff wrote that "savings require: (i) further pension reform; (ii) additional efforts to rein in health care expenditures; (iii) enhancements in public expenditure efficiency; and (iv) tighter unemployment benefits" (p. 24-25). IMF staff expressed repeated concerns over the aging of the population in the report and wrote "pension reform is key to contain the fiscal costs of aging" (p. 16). Staff recommended raising the retirement age from 65 to 67 years. To rein in health care expenditures, staff recommended "an increase in user fees" to moderate healthcare demand growth (p. 16). To tighten unemployment benefits "staff suggested lowering [maximum unemployment benefit duration] to 18 months" from the current 38 months (p. 17).

The 2009 Article IV consultation report observed that "the Netherlands has been dealt a severe blow by the global crisis," (p. 5) and IMF staff viewed "the fiscal relaxation [to be] appropriate" (p. 4). But staff expressed concerns over "the significant contribution of recurrent spending to the ongoing fiscal loosening will prove difficult to reverse when growth picks up" (p. 6). Therefore, "fiscal adjustment targets for 2012-15 and supporting measures should figure prominently in the coalition agreement that will emerge from the 2011 elections" (p. 6). Expenditure-based consolidations were considered "more durable," and preferred over taxes; where "health and old-age-care reforms are crucial to containing—particularly aging related —expenditure" (p. 6). Specific recommendations were curtailing aging-related expenditures, including raising the retirement age, relying more on means-testing and second pillar pensions, increase user fees to restrain health-services demand, and tighter definition of long-term care entitlements (p. 6). At the same time, labor market policy recommendations focused on increasing "labor participation, especially for female and elderly work" (p. 4).

In the 2011 Article IV consultation, IMF staff welcomed the Netherland's commitment to consolidation, and advocated adjustment of about ¾ percent of GDP per annum beyond 2015 (p. 23). But staff warned that "historical experience indicates that negative effects on demand from budget consolidation are likely to be higher when monetary policy is not able to accommodate tightening, as is currently the case" (p. 21). IMF staff further argued that expenditure retrenchment should play a key role in adjustment. "Expenditure-based consolidations have generally been more successful, based on international evidence" (p. 25). "The priority should be reducing the impact of aging on fiscal expenditures, through increases in the effective retirement age and measures to restrain growth in demand for health- and long-term care" (p. 25). The focus on the revenue side should be on "curtailing generosity of MID [mortgage interest deduction]" and shifting taxation "from labor to less distortionary taxation of consumption and property" (p. 25).

Social policy recommendations focused on "increasing the retirement age," "overhaul [of] tax and benefit systems to curtail disincentives to full-time female and elderly work," "excessive generosity of unemployment benefits should be pared down," "fostering research and development (R&D) expenditure to enhance productivity" (p. 29). Furthermore, IMF staff recommended "stepp[ing] up investment in roads and railways" to alleviate congestion and spur productivity" (p. 26). Underlying requirements for investment in infrastructure mentioned by were relaxation of strict zoning regulation, road pricing, and more competition in the transportation industry (p. 27, 29).

Poland

In 2009, Poland's economy was doing well. "The economy has continued to expand even as all neighboring countries and most CEE [Central and Eastern Europe] peers have been mired in deep recession" (p. 26). The 2009 Article IV consultation supported "cautiously easing monetary policy" and increasing the deficit limit in the short term (p. 18, 15). The report noted that "having entered the crisis without serious internal or external imbalances, the authorities were afforded some room to undertake counter-cyclical measures" (p. 1). However, IMF staff recommended that Poland adopts "binding multi-year expenditure limits" to bolster confidence in consolidation in the medium term (p. 15). Staff further proposed social reforms in the medium term to reduce the deficit, such as "better targeting child deductions…, disability contributions, and pension indexation" (p. 16). The greatest concern expressed in the consultation report was Poland's labor supply shortages. The report noted: "the evidence that growth had begun to falter even before the onset of the global crisis because of emerging labor shortages should serve as an important reminder of the urgency of [boosting Poland's labor force participation rate]" (p. 28). IMF staff recommended "increasing the effective retirement age and equalizing the statutory retirement age of men and women" (p. 22).

Poland "is the only EU country to have escaped a recession in 2009 due to its limited reliance on exports, well-capitalized and profitable banking system, flexible exchange rate, and limited pre-crisis imbalances" (p. 1). In the 2010 Article IV consultation, IMF staff credited "the highly counter-cyclical fiscal policy [as being] a main reason for Poland's [economy] having avoided a recession" (p. 25). The staff found Poland's deficit target of 3 percent of GDP by 2012 to be "too ambitious," and proposed meeting the target by 2013-14 (p. 18, 25). Furthermore, staff recommended "adopt[ing] a permanent, binding expenditure rule with a deficit or debt anchor" (p. 19). In the staff's assessment, "substantial fiscal adjustment needed over the medium term will require changes in entitlement programs" (p.19). Options proposed included "tightening pension indexation, rationalizing other benefits (sickness, disability, etc.), and increasing the flexibility of limits on defense spending," along with "further revenue-enhancing measures" (p. 19). In terms of monetary policy, "staff believes that a rise in policy rates would not be warranted any time soon" (p. 22). They proposed "limited foreign-exchange interventions," and discouraged "early euro adoption" (p. 1, 24, 26).

By 2011, Poland was on the path to archive the deficit goal. The 2011 Article IV consultation report noted: "on staff's baseline projections, the fiscal deficit would fall over the medium term to 2 percent of GDP… To reduce debt firmly over time, the fiscal deficit should be cut to no more than 1 percent of GDP over the medium term" (p. 8). IMF staff reiterated the recommendation of reforms of entitlement programs and structural reforms to increase labor force participation rates, including raising the retirement age and tightening indexation (p. 9, 14). Due to growing concerns about inflationary pressures, staff advised "some further gradual hikes in the policy rate will be needed to bring inflation back to target" (p. 11, 15). Finally, "euro adoption remains an important long-term objective" (p. 15).

Portugal

In the 2008 Article IV consultation, IMF staff observed that "despite impressive recent consolidation, Portugal's fiscal situation remains weak, and consolidation needs to continue in 2009" (p. 18). Staff advised that "structural consolidation should be at least a ½ percent of GDP," and "beyond 2009, additional measures of about 1 percent of GDP will likely be needed to reach the MTO [medium-term objective]" (p. 18). "At the root of Portugal's economic problems," staff argued, "lies anemic productivity growth and a significant external competitiveness gap" (p. 3). Therefore "further reform should focus on making the economy more flexible and competitive" (p. 3). This would include reconsidering "higher rate of social security contributions on fixed-term contracts," "implement the EU Services Directive to make a clean sweep of regulations at all levels of government," and "strengthening judicial system efficiency" to support the effectiveness of the Competition Authority (p. 3, 27). The IMF did not conduct Article IV consultations for Portugal in 2010 and 2011.

Romania

The 2010 Article IV consultation focused on fiscal consolidation in the form of spending cuts in the medium term. "With continued reductions in public employment and the enactment of pension, health and education reforms, the deficit would remain on a downward path to fall below the 3 percent Maastricht threshold in the medium-term without the need for major tax increases." (p. 30) Staff identified three "key elements in the medium-term fiscal adjustment strategy: 1) "pension reform;" 2) "reforms to permanently rein in the wage bill;" and 3) "reforms of social spending" (p. 21-22). To reduce social spending, IMF staff recommended "reforming social assistance programs, streamlining the number of programs and improving the targeting and incentives in the remaining ones" (p. 22). While pension reforms should include "build[ing] up the pillar two private pension system." (p. 22)

Pension and educational reforms were also seen a means to increase potential growth. "Lifting the Romanian employment rate… while reforming the early retirement schemes would boost potential growth by about 0.6 percentage points, help with fiscal sustainability, and pensions costs" (p. 26). Proposed "labor reforms should include helping low-skilled workers enter the job market and promoting senior labor" (p. 26). The consultation report did not offer any specific recommendations on education reform, but agreed with the education reform under consideration of setting a nationwide standard wage for teachers, increasing teaching hours per teacher and decentralizing decisions (p. 27).

Slovakia

The 2009 Article IV consultation discussed the key challenge for fiscal policy "to anchor an accommodating fiscal stance during the recession within a credible medium-term consolidation strategy" (p. 9). The staff argued for bringing down the deficit to below 3 percent of GDP by 2011. "To achieve the recommended deficit path, a combination of expenditure and revenue measures should be considered" (p. 9). Specific recommendations included "additional health care reform," "wage growth moderation in the public sector," "broaden the base of social security contributions," and "higher taxes on income" (p. 9). Moreover, the staff stated that "productivity-enhancing structural reforms, wage discipline, and labor market flexibility should remain policy priorities" (p. 16). Specifically, "the government should continue to improve the business environment and place special focus on strengthening the education system" (p. 16).

By 2011, "Slovakia [had] swiftly recovered from a deep recession" (p. 1). The 2011 Article IV consultation report predicted that the country "is facing a favorable medium-term macroeconomic outlook" (p. 1). Staff's views were that "fiscal consolidation should continue with the aim of reducing the deficit to below 3 percent of GDP in 2013;" and "fiscal adjustment efforts need to continue beyond 2013" (p. 12). The staff recommended "capping expenditure growth in real terms for 2012-15 [to] set a consolidation path toward a deficit of 1 percent of GDP" (p. 13). Nonetheless, "in spite of the strong recovery,… long-term unemployment of low-skilled and young workers has risen to among the highest in the EU" (p. 1). "More than one out of three workers under 25 was unemployed" (p. 24). The staff commended the Slovak authorities on their new labor market policy initiatives, but proposed further focusing training, education and vocational programs toward labor market needs (p. 24-25). Moreover, "differentiating the minimum wage among regions… could help strengthen employment incentives," and "improving the transport infrastructure and private rental market could help ease labor mobility constraints" (p. 25). To maintain competiveness, the staff advised productivity gains, labor market flexibility and wage growth moderation (p. 25).

Slovenia

By spring of 2009, "Slovenia's economy [was] increasingly affected by the global crisis" (p. 1). In the 2009 Article IV consultation, "the authorities and staff concurred that a fiscal stimulus [was] necessary," and staff supported a fiscal stimulus of 2.1 percent of GDP (p. 10). However, "staff stressed that the fiscal position should be reverted to a more conservative stance as the crisis subsides" (p. 11). Where "fiscal adjustment should mainly come through the consolidation of expenditures" (p. 11). To achieve long-term fiscal sustainability, the staff recommended pension reform that would "de-link[] pensions from wages and increase[e] the retirement age" (p. 12). The staff also expressed concerns over Slovenia's competitiveness having deteriorated as a consequence of large devaluations in neighboring countries, and argued for "further liberalization of employment protection legislation [being] necessary in the medium term and could be implemented in the context of a 'flexicurity' approach" (p. 12). Staff disagreed with Slovenia's work-sharing stimulus initiative, arguing that it was not "sufficiently targeted to the most vulnerable groups,… might entail a risk of abuse, and would be hard to reverse if the crisis continues" (p. 11).

Slovenia experienced "one of the largest GDP declines in the euro area" (p. 1). The 2011 Article IV consultation discussed "putting growth and public finances on a sustainable path." (p. 1) IMF staff argued that "while general government debt is likely to remain sustainable, fiscal consolidation is necessary in light of the uncertainty in financial markets and contingent liabilities" (p. 8). Where "consolidation should take place on the expenditure rather than the revenue side" (p. 8). Among the expenditure measures proposed were no new increases in the public sector wage bill, "rationalizing government employment; and reforms to strengthen the targeting of transfer programs and tighten eligibility" (p. 9). Pension reform proposals focused on "reducing the replacement rate and increasing… retirement age" (p. 9). "Finally, the private pillar should be expanded to compensate for the public benefit cuts" (p. 9). The staff found that "structural reforms in the labor and product markets [were] critical to boost potential growth" (p. 20). Slovenia's "unemployment compares favorably to other euro area countries. However, the many job losses in the construction sector are probably permanent… Labor market flexibility should therefore be increased" (p. 15-16). Staff recommended loosening of "labor market restrictions – especially for dismissals," "cancelling any remaining indexation of the minimum wage and eliminating the mandatory wage supplement for years of service" (p. 20).

Spain

By early 2009, "Spain [had] entered a sharp downturn" (p. 1). The 2008 Article IV consultation, released in February 2009, cautioned "fiscal policy needed to remain cautious given that some fiscal powder also should be kept dry, as a contingency, to assist banks with capital, if needed" (p. 27). Staff calculated that Spain's public sector net worth would drop to -147 percent of GDP in 2009, and therefore "Spain has no fiscal space for expansion, unless the authorities commits to adjustments" (p. 30). If "further fiscal support were needed, staff stressed that this should be combined with long-run fiscal, labor (such as agreeing with social partners on a program of wage moderation and labor market liberalization), and product market reforms" (p. 27). Structural macroeconomic labor reform recommendations were "elimination of wage indexation, earlier adoption of opt-out clauses from bargaining contracts…, and a reduction in the segmentation of labor markets between fixed-time and full-time contracts" (p. 39). Staff also recommended framing fiscal policies in the long run context of sustainability to strengthen confidence to "avoid private agents from turning Ricardian" (p. 39). Sustainable fiscal adjustments proposed were "parametric pension and health reforms; extending retirement ages; limiting benefit indexation for the wealthiest; a combination of progressive income tax increases and expenditure cuts…, [and] phasing out the mortgage interest deduction" (p. 31-2).

In the 2010 Article IV consultation, IMF staff noted that "the necessary adjustment is underway and output has stabilized" (p. 1). The staff endorsed Spain's "ambitious fiscal consolidation to reach the 3 percent of GDP deficit target by 2013" (p. 13). The staff argued that "empirical evidence also suggests that recoveries from economic crises often serve as an opportunity for reform" (p. 13). Specifically, "Spain needs a bold pension reform" including "raising the retirement age, [and] increasing incentives to work in old age… to help bolster sustainability" (p. 17). IMF staff's assessment of the labor market was that "the labor market is not working" (p. 19). Therefore, the staff argued that "a radical overhaul of the dysfunctional labor market is urgent" (p. 20). Specific proposals to make labor markets more flexible included "lowering severance payments," and "reduc[ing] protection of permanent contracts with decentralized wage setting and eliminating indexation" (p. 20, 25).

By 2011, the Spanish "economy [was] gradually recovering and rebalancing is underway." (p. 28) But "the recovery has not been enough to reduce very high levels of unemployment" which were around 21 percent (p. 9). The 2011 Article IV consultation report noted that "Spain's unemployed need a decisive improvement in employment prospects" (p. 26). Therefore, "policy should thus err on the side of boldness rather than gradualism" (p. 26). IMF staff recommended "collective bargaining needs to be effectively decentralized to the firm level," "social partners should move away from inflation indexation," "severance payments should be further lowered," and "improving retraining of workers with mismatches skills, supporting youth employment, and ensuring that the incentives to return to work are sufficient" (p. 26).

The IMF staff commended the Spanish authorities on their fiscal consolidation plans, but cautioned "deficit target path [cutting the deficit to 2.1 percent of GDP by 2014 from 9.2 percent in 2010] is appropriate, but… is based on relatively optimistic macroeconomic projections" (p. 20). The staff argued that additional measures may be required, including "further reducing current spending" (the public wage bill)," "cutting investment," and "raising…VAT and excise rates" (p. 21). To address longer-term spending pressures, the staff urged "the government [to] commit to an early date to archive the MTO [medium-term objective] of a balanced budget and pro-actively manage below-the-line operations (such as privatization)" (p. 30). Moreover, "pension reform should also be quickly passed and implemented, and ideally strengthened in some areas" (p. 30).

Sweden

"Up until the spring of 2008, the Swedish economy boomed" (2009: p. 3). However, "Sweden has been hit hard by [the international financial wholesale markets] crash" (p. 3). IMF staff assessed that "the authorities' response was prompt and appropriate," and "monetary policy is appropriate" (p. 3, 4). Most of the 2009 Article IV consultation addressed short-term policies with the "immediate prospects for recovery [being] at the mercy of developments abroad" (p. 3). A medium-term recommendation was that "the target of a surplus of 1 percent of GDP over the cycle should remain, as should firm commitment to the nominal spending ceilings" (p. 4).

In the 2010 Article IV consultation, IMF staff provided little fiscal and monetary policy advice. They stated that that "the current fiscal rules -- targeting a surplus of 1 percent of GDP across the cycle, supported by medium-term expenditure ceilings – remain[ed] well suited for Sweden" (p. 36). The 2010 report also assessed the labor market situation, noting that "the labor market has held up much stronger than expected" (p. 32). IMF staff commended Sweden for making more resources available for "preparatory and vocationally-oriented training, and improved information for job seekers regarding vacancies" (p. 32).

By 2011, "Sweden ha[d] recovered strongly from the global recession" (p. 3). The IMF Article IV consultation report found that "Sweden's exit from the global crisis has been uniquely successful compared to others in the European Union" (p. 24). Nonetheless, "the output gap – however measured – was well below expectations, as was unemployment" (p. 11). Recommendations in the 2011 consultation on fiscal and monetary policies focused on the shorter term, specifically, "the underlying fiscal stance should remain unchanged;" (p. 24) and "the monetary stance should continue to tighten in 2011" (p. 25). The consultation further discussed labor markets in some detail. IMF staff recommended "moderate settlements in the 2011-12 wage round – in the neighborhood of 3 percent" (p. 25). In order "to drive unemployment down to 5 percent on a sustained basis", "policies should continue to reduce unemployment rates without lowering adult participation rates" (p. 15). Specific proposals were "lowering labor market frictions, including impediments to matching," and "the introduction of permanent concessionary wage determination arrangements for new entrants to the labor market" (p. 15, 16).

United Kingdom

One of the main concerns discussed in the 2008 Article IV consultation was inflation. (Following the release of the consultation on July 7, 2008, the IMF released a supplement to the report on July 25, 2008). In the supplement, IMF staff wrote that "the case for strengthened policies remains. Long-run inflation expectations have risen further" (p. S4). IMF staff recommended "a monetary stance that remains focused on the inflation target," (p. 4) and "remain[s] firmly focused on price stability" (p. 22). The report stated that "tight monetary policy and subdued growth will be required to prevent elevated inflation expectations from getting embedded into wages and prices" (p. 22). To keep inflation expectations in check, "continued moderation in nominal earnings growth will be essential," but staff noted that "tolerance for ongoing low real earnings growth is uncertain with continued tight labor markets" (p. 4). In terms of fiscal policy, IMF staff recommended the "40 percent net debt ceiling should be retained," and if the 40 percent is breached, "concrete plans to bring it back under the ceiling on a sustained basis should be announced promptly" (p. S4, 5). In order to rebalance demand, and adhere to the debt rule, IMF staff noted that "budget consolidation will be essential" (p. 21). IMF staff calculated that "it would take an adjustment averaging ¾ a percentage point of GDP per year… to set debt on a path to return under the ceiling by 2012" (p. S4). Moreover, the staff made the case for "nominal expenditure ceilings." (p. S4) "Nominal spending caps are simple and transparent" (p. 33). Finally, "if the medium-term outlook for the current account deteriorates, additional structural fiscal consolidation may be needed 2009 and beyond" (p. 4).

By 2009, "the United Kingdom [had] been hit hard by the global financial crisis" (p. 4). Inflation was no longer a threat as "inflation [was] set to continue falling and remain below target for some time" (p. 31). The 2009 Article IV consultation stressed that "a strong commitment to medium-term fiscal consolidation is crucial," (p. 38) as "the success of the current policy package hinges on continued trust in the sustainability of the fiscal position" (p. 6). IMF staff recommended that the focus of a fiscal consolidation plan be "on putting public debt on a firmly downward path faster than envisaged… and to weigh the adjustment toward expenditure reduction" (p. 6). The consultation does not provide specifics on expenditure-based consolidation other than mentioning "implementing structural reforms to address the rising costs related to demographic change, especially in health care" (p. 39).

By 2010, the staff's assessment was that the "UK economy [was] on the mend, but crisis-related scars still needed healing" (p. 42). In the 2010 Article IV consultation report, IMF staff wrote: "although this consolidation effort involves painful decisions and dampens short-run growth, it is necessary to enhance credibility and ensure fiscal sustainability." (p. 26) The staff commended the UK authorities for the fiscal mandate of balancing the cyclically-adjusted current budget over a five-year rolling horizon (p. 26). Emphasis should be on spending reduction and "more weight should be given to reducing public sector compensation premia and achieving savings in benefits and transfers through better targeting" (p. 43). In order to bolster fiscal sustainability, "entitlement reforms to address long-term fiscal challenges should be pursued" (p. 30, 43). Specifically, the UK should accelerate "the planned increases in statutory retirement age for state pensions and gradually aligning the generosity of public pensions" (p. 31). With regards to monetary policy, staff noted that "a highly accommodative monetary stance remains appropriate" (p. 42). "If a stalling recovery were to heighten disinflationary forces, quantitative easing should be expanded" (p. 37). On the other hand, gradual tightening is needed with the prospect of above-target inflation (p. 38).

In 2011, the economic "recovery stalled…inflation remains elevated, and unemployment is still unacceptably high" (p. 1). The 2011 Article IV consultation focused primarily on evaluating the economic situation and authorities' policy plans (p. 5). The IMF stressed that the strong fiscal consolidation underway was "essential to achieve a more sustainable budgetary position, thus reducing fiscal risks" (p. 1). As growth resumes, withdrawal of monetary policy through policy rate hikes and asset sales should be gradual (p. 31). IMF staff found the UK path of consolidation appropriate, but recommended further structure reforms to address remaining longer-term fiscal imbalances and support medium-term growth, including "accelerating increases in the state pension age and indexing it to longevity," "reforming public-service pensions," "easing tight planning restrictions" to increase new real estate developments" (p. 36-37).

Conclusion

This content analysis of IMF article IV consultations in the European Union shows a consistent pattern of recommendations on fiscal policy as well as policies concerning employment and social protections. There is an overwhelming emphasis on fiscal consolidation, reduction of social expenditures, as well as measures that would weaken the bargaining power and income of labor, and make it more difficult for governments to promote growth and employment or reduce poverty and social exclusion. The findings herein confirm prior research on IMF Article IV consultations in other countries, including most recently Islam et al. (2012). That analysis, which looked at 50 Article IV consultations for developing countries, found similar predilections with regard to fiscal consolidation and other "one-size-fits-all" policies that were not necessarily appropriate for these developing countries.

It is difficult to measure the influence of the Article IV consultation process and papers, but clearly they are important. In many cases we can see that the recommended measures are adopted, even against considerable political resistance – for example, the comprehensive labor law reforms in Spain, which weakened industry-wide collective bargaining and employment protections; and public pension cuts in Italy. These were countries that did not have a lending agreement with the IMF. The Article IV papers are also read by financial analysts and can play an important signaling role to financial markets.

Of course, IMF policy recommendations carry more weight with smaller countries in the EU (countries such as Germany and France are likely to feel less pressure to follow their advice); and they carry the most weight of all in borrowing countries, since their financial stability is at risk if they do not follow IMF advice. As noted above, the impact of IMF policy recommendations in these countries (e.g. Greece, Ireland, Latvia, and Portugal) is not completely captured in the Article IV papers examined here, and may have had a large impact on the prolonged crisis in Europe.

The IMF now has the majority of its loans in EU countries, a portfolio that is drastically different than just a few years ago. (IMF 2012c: Table 2a; IMF 2012d: Table 3a) It should be noted that the IMF's decisions and recommendations in Europe are overwhelmingly influenced by the European governments who sit on its Board of Governors and Executive Board, and especially the larger countries. This is somewhat different than its decision-making in developing countries. In Latvia, for example, there is evidence that IMF economists did not favor the enormously costly (in terms of lost output and employment) "internal devaluation" strategy that it agreed to and was implemented.[11] Nonetheless, the IMF is by virtue of its lending and role, an important member of the so-called "Troika" that is deciding and implementing policy in the borrowing countries in the eurozone, as well as influencing policy throughout the European Union.

As noted above, since – as some economists have argued – policy mistakes have played a major role in the prolonged economic crisis and current recession in Europe, IMF policy recommendations in this region deserve special attention. Because of Europe's current influence on the problems of the global economy and the apparent struggle between the Troika and eurozone governments over what kinds of "reforms" will be necessary to get the authorities' cooperation in putting an end to the crisis, the reform agenda represented in these Agreements takes on a special importance. That agenda has proven deeply unpopular, and has contributed to the fall of many European governments in the past three years.

The reform agenda represented in these agreements appears also to conflict with other goals that the European Union has agreed upon, for example the goals represented by Europe 2020. It is difficult to see how research and development expenditures can be increased to 3 percent of GDP, for example, or the number of people at risk of poverty and social exclusion can be reduced to meet the Europe 2020 targets, if fiscal consolidation and cuts to social expenditures continue. Even the climate change goals will be more difficult to reach without the means for public investment in

11 Weisbrot and Ray 2011: 8; and also see statement by Anders Aslund in Weisbrot 2012.

reducing fossil fuel consumption. All of these goals, as well as the necessary economic recovery from the regional recession, are also in conflict with the Fiscal Compact signed in March 2012, which provides for further tightening of fiscal policies and more mechanisms to enforce this tightening. The IMF's agenda in these Article IV consultations is in line with the Fiscal Compact, but not with the economic and social goals of Europe 2020.

There has been much debate over the role of IMF surveillance since the IMF's admitted failure to apprehend the risks to the global economy in the run-up to the Great Recession. The IMF's Independent Evaluation Office issued a report noting that the IMF "fell short" in its "most important purpose" of "warning member countries about risks to the global economy and the buildup of vulnerabilities in their own economies," and that this failure was due to such factors as "a high degree of groupthink; intellectual capture," and "an institutional culture that discourages contrarian views,"… "while political constraints may have also had some impact" (Independent Evaluation Office 2012: p. vii, 1).

The IMF (2011) produced recommendations for improvement in its 2011 Triennial Surveillance Review. There has been a noticeable improvement in the IMF's multi-lateral surveillance and risk assessment in the past few years. There has also been a wider range of views on macroeconomic policy issues expressed within the research department of the IMF than there was before the Great Recession.

However, this review of Article IV agreements shows that there has been little change in the IMF's policy advice to European countries. It also supports the view that policy mistakes by the European authorities – including here the IMF's overwhelming priority of fiscal consolidation – have unnecessarily prolonged and deepened the crisis in Europe, and contributed to a reform agenda that worsens the impact of the crisis on vulnerable parts of the population.

The content analysis in this paper suggests that the IMF might wish to engage in an IEO review of its policy advice in Europe, similar to its review of the IMF's surveillance in the run-up to the Great Recession and its review of the IMF's policies during the Asian economic crisis of the late 1990's. Both of these reports found serious mistakes and led to significant changes in both research and policy at the IMF. Given the urgency of the present situation in Europe, an expedited review of current policy might enable the IMF to play a constructive role in Europe's recovery. At the same time, it will also demonstrate the IMF's commitment to the goals of accountability and transparency in its role as 'trusted advisor.[12]

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12 This is the expression used by the IEO. It is finalizing an evaluation on the theme of 'The role of the IMF as Trusted Advisor'. See IEO (2012) 'Dialogue', Fall, available at http://www.ieoimf.org/ieo/files/newsletter/newsletter_fall_2012.pdf.

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Appendix A

List of IMF Article IV Consultations

Austria		2008	2009		2011
Belgium		2008	2009	2010	2011
Bulgaria		2008		2010	2011
Cyprus			2009		2011
Czech Republic	2008,		2010	2011	
Denmark		2008		2010	
Estonia		2008	2009	2010	2011
Finland		2008		2010	
France				2009	2010
Germany		2008		2010	2011
Greece				2009	
Hungary		2008		2010	2011
Ireland			2009	2010	
Italy			2008		2010
Latvia					2010
Lithuania			2009	2010	
Luxembourg			2009	2010	2011
Malta					2010
Netherlands		2008	2009		2011
Poland				2009	2010
Portugal		2008			
Romania				2010	
Slovakia			2009		2011
Slovenia			2009		2011
Spain			2009		2010
Sweden			2009	2010	2011
United Kingdom	2008	2009	2010	2011	