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Recommendation for a

COUNCIL RECOMMENDATION

on the 2018 National Reform Programme of Estonia

and delivering a Council opinion on the 2018 Stability Programme of Estonia

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THE COUNCIL OF THE EUROPEAN UNION,

Having regard to the Treaty on the Functioning of the European Union, and in particular Articles 121(2) and 148(4) thereof,

Having regard to Council Regulation (EC) No 1466/97 of 7 July 1997 on the strengthening of the surveillance of budgetary positions and the surveillance and coordination of economic policies[1], and in particular Article 5(2) thereof,

Having regard to the recommendation of the European Commission[2],

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

Having regard to the conclusions of the European Council,

Having regard to the opinion of the Employment Committee,

Having regard to the opinion of the Economic and Financial Committee,

Having regard to the opinion of the Social Protection Committee,

Having regard to the opinion of the Economic Policy Committee,

Whereas:

(1) On 22 November 2017, the Commission adopted the Annual Growth Survey, marking the start of the 2018 European Semester of economic policy coordination. It took due account of the European Pillar of Social Rights, proclaimed by the European Parliament, the Council and the Commission on 17 November 2017. The priorities of the Annual Growth Survey were endorsed by the European Council on 22 March 2018. On 22 November 2017, on the basis of Regulation (EU) No 1176/2011, the Commission also adopted the Alert Mechanism Report, in which it did not identify Estonia as one of the Member States for which an in-depth review would be carried out. On the same day, the Commission also adopted a recommendation for a Council recommendation on the economic policy of the euro area, which was endorsed by the European Council on 22 March 2018. On 14 May 2018, the Council adopted the recommendation on the economic policy of the euro area ('recommendation for the euro area').

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1 OJ L 209, 2.8.1997, p. 1.
2 COM(2018) 406 final.
3 P8_TA(2018)0077 and P8_TA(2018)0078.

(2) As a Member State whose currency is the euro and in view of the close interlinkages between the economies in the economic and monetary union, Estonia should ensure the full and timely implementation of the recommendation on the economic policy for the euro area, as reflected in the recommendations below, in particular (1).

(3) The 2018 country report for Estonia[4] was published on 7 March 2018. It assessed Estonia's progress in addressing the country-specific recommendations adopted by the Council on 11 July 2017, the follow-up given to the recommendations adopted in previous years and Estonia's progress towards its national Europe 2020 targets. The Commission's analysis leads it to conclude that Estonia is not experiencing macroeconomic imbalances.

(4) On 26 April 2018, Estonia submitted its 2018 National Reform Programme and its 2018 Stability Programme. To take account of their interlinkages, the two programmes have been assessed at the same time.

(5) Relevant country-specific recommendations have been addressed in the programming of the European Structural and Investment Funds for the 2014-2020 period. As foreseen in Article 23 of Regulation (EU) No 1303/2013 of the European Parliament and of the Council[5], where it is necessary to support the implementation of relevant Council recommendations, the Commission may request a Member State to review and propose amendments to its Partnership Agreement and relevant programmes. The Commission has provided further details on how it would make use of that provision in guidelines on the application of the measures linking the effectiveness of the European Structural and Investment Funds to sound economic governance[6].

(6) Estonia is currently in the preventive arm of the Stability and Growth Pact. The government plans to move from a general government deficit of 0.3 % of GDP in 2017 to a surplus of 0.2 % of GDP in 2018, 0.5 % of GDP in 2019 and move towards a balanced budget thereafter. Its medium-term budgetary objective is a structural deficit of 0.5 % of GDP. According to the 2018 Stability Programme, the recalculated[7] structural deficit is projected to amount to 0.8 % of GDP in 2018, 0.4 % of GDP in 2019 and remaining in a slight deficit thereafter. The general government debt-to-GDP ratio is projected to remain below 9 % of GDP in 2018 and 2019, declining to 5.3 % of GDP by 2022. The macroeconomic scenario underpinning those budgetary projections is favourable. Negative risks for the revenue yield assumptions primarily relate to some of the measures which are not well specified, affecting all years of the programme horizon.

(7) For 2018, Estonia was recommended to remain at the medium-term budgetary objective. This is consistent with a maximum nominal growth rate of net primary government expenditure[8] of 6.1 %, corresponding to an allowed deterioration in the

[4] SWD(2018) 205 final.

[5] Regulation (EU) No 1303/2013 of the European Parliament and of the Council of 17 December 2013 laying down common provisions on the European Regional Development Fund, the European Social Fund, the Cohesion Fund, the European Agricultural Fund for Rural Development and the European Maritime and Fisheries Fund and laying down general provisions on the European Regional Development Fund, the European Social Fund, the Cohesion Fund and the European Maritime and Fisheries Fund and repealing Council Regulation (EC) No 1083/2006 (OJ L 347, 20.12.2013, p. 320).

[6] COM(2014) 494 final.

[7] Cyclically-adjusted balance net of one-off and temporary measures, recalculated by the Commission using the commonly agreed methodology

[8] Net primary government expenditure comprises total government expenditure excluding interest expenditure, expenditure on Union programmes fully matched by Union funds revenue and non-discretionary changes in unemployment benefit expenditure. Nationally financed gross fixed capital

structural balance by 0.2 % of GDP. Based on the Commission 2018 spring forecast there is a risk of some deviation from that requirement in 2018. In 2019, in view of Estonia's projected output gap of 2.7 % and with projected GDP growth below to the estimated potential growth rate, the nominal growth rate of net primary government expenditure should not exceed 4.1 %, in line with the structural adjustment of 0.6 % of GDP stemming from the matrix of requirements under the Stability and Growth Pact. Based on the Commission 2018 spring forecast under unchanged policies, there is a risk of some deviation from that requirement in 2019 and over 2018 and 2019 taken together. Overall, the Council is of the opinion that Estonia needs to stand ready to take further measures to ensure compliance in 2018 and 2019.

(8) Providing a more adequate social safety net supported by better service provision remains a major challenge for Estonia. Estonia spends less on social protection (around 16 % of GDP) than the European Union average (around 28 % of GDP). The impact of social transfers on reducing poverty is improving but still weak and below the European Union average. Estonia still has a high at-risk-of-poverty rate, particularly for people with disabilities, jobless households and older people, especially those living alone. Income inequality at 5.6 % in 2016 remains higher than the European Union average (5.2 % in 2016) despite recent improvements. Some steps are being taken to provide adequate family benefits for larger families, which has further reduced relative poverty among children. The level of minimum income benefit was increased, accompanied by incentives to return to work. The payment of an allowance of EUR 115 to persons with low pensions and living alone was the first step in addressing the very high at-risk-of-poverty rate of this group. The at-risk-of-poverty-or-social-exclusion gap between people with disabilities and those without (20.9 % in 2016) was also higher than the European Union average (10.1 %). Financing of long-term care services does not match the needs of the ageing population. The impact of ongoing administrative reform on the delivery of high quality services remains to be seen.

(9) The gender pay gap remains one of the highest in the European Union at 25.3 % although it is reducing. Work-life balance is being promoted by the recent changes to the parental leave and benefit system. These changes are expected to give women an incentive to return to work earlier and thereby contribute to lowering Estonia’s gender pay gap. The changes will be implemented between 2018 and 2020. The proposal on the second stage of parental leave reform is being discussed. Continued engagement with social partners and strengthening their capacity, in light of very low membership rates, remain important in this context and beyond. Amendments to the Gender Equality Act to improve wage transparency have yet to be adopted and, once adopted, will only apply to the public sector entities. A tool to analyse wage differences between genders is not expected to be developed before 2019.

(10) Estonia’s slow productivity growth is linked to its moderate performance on research, technology and innovation. With less than 0.5 % of Estonian companies reporting research activities in 2016, business research and development intensity is only 0.7 % of GDP — half the EU average of 1.3 %. In addition, several indicators measuring innovation — such as small and medium-sized companies creating new products and processes or innovating in-house — have declined significantly in recent years. While the economy has some high value added and knowledge-intensive activities, business

formation is smoothed over a 4-year period. Discretionary revenue measures or revenue increases mandated by law are factored in. One-off measures on both the revenue and expenditure sides are netted out.

research and development intensity, science-business links, and companies' innovation and technological capacity remain low. Public sector expenditure on research, technology and innovation has traditionally been above the European Union average. However, insufficient priority-setting in public research poses challenges. Estonia has put in place several measures to boost the economy's research and innovation performance, but it is a challenge to maximise their impact.

(11) In the context of the 2018 European Semester, the Commission has carried out a comprehensive analysis of Estonia's economic policy and published it in the 2018 country report. It has also assessed the 2018 Stability Programme and the 2018 National Reform Programme and the follow-up given to the recommendations addressed to Estonia in previous years. It has taken into account not only their relevance for sustainable fiscal and socioeconomic policy in Estonia but also their compliance with Union rules and guidance, given the need to strengthen the Union's overall economic governance by providing Union-level input into future national decisions.

(12) In the light of this assessment, the Council has examined the 2018 Stability Programme and its opinion[9] is reflected in particular in recommendation 1 below.

HEREBY RECOMMENDS that Estonia take action in 2018 and 2019 to:

1. Ensure that the nominal growth rate of net primary government expenditure does not exceed 4.1 % in 2019, corresponding to an annual structural adjustment of 0.6 % of GDP. Improve the adequacy of the social safety net, in particular for older people and people with disabilities. Take measures to reduce the gender pay gap, including by improving wage transparency in the private sector.

2. Promote research and innovation, in particular by providing effective incentives for broadening the innovation base.

Done at Brussels,

For the Council
The President

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