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Lifting Euro Area Growth: Priorities for Structural Reforms and Governance

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EXECUTIVE SUMMARY

To live up to its growth potential and secure its inclusive social model, the euro area must make better use of its available labor. *In the aftermath of the crisis, boosting growth is essential to prevent unemployment from becoming a long-term problem and to facilitate the return to fiscal sustainability. Labor utilization in the euro area has been lagging considerably behind its best performing peers. While fewer hours worked may, to some extent, reflect a social choice, higher unemployment rates and lower participation rates, on the other hand, cannot easily be attributed to individual preferences. Here, policies and institutions matter more. And there is little excuse for relatively low labor productivity, a particular bane in southern Europe and an increasing challenge everywhere.*

Kick-starting growth requires a comprehensive approach to labor and service market reforms. *Different circumstances call for different approaches across countries. Countries in southern Europe need to focus on regaining competitiveness, while some in the core should promote higher labor force participation or more open service sector markets. Improving access to the labor market should be high on the priority list everywhere—including through some harmonization of key features of the labor market, which will help deal with intra-euro area imbalances. Differences in labor taxation, unemployment benefit systems, and employment protection will need to be reduced. Improving regulation and reforming taxes and social benefits will be essential to make inroads. For the longer term, focus should be on innovation, education, and on continuing financial sector reforms.*

Strong impetus for reforms will benefit from strengthened coordination. *In the past, reforms have succeeded when the agenda was driven by European institutions and a common sense of destiny, but largely failed when reliant on peer pressure. Recent steps and proposals to strengthen governance over both fiscal and structural policies at the euro area level go in the right direction. More reform authority should be vested at the euro area level and countries should be willing to adjust national policies to secure an effective functioning of the economic and monetary union. In particular, key structural reforms need to be embedded in a stronger surveillance mechanism over fiscal and structural policies; EU transfer rules revised to better reward reformers and punish laggards; and compliance enforced more decisively than in the past. Launching a new common project for labor market reform would be beneficial.*