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Council closes excessive deficit procedures for Czech Republic, Italy, Portugal and Slovakia

The Council today[1] adopted decisions, under article 104(12) of the treaty, abrogating decisions it took in 2004 and 2005, under article 104(6) of the treaty, on the existence of excessive government deficits in the Czech Republic, Italy, Portugal and Slovakia.

This follows reduction by all four countries of their government deficits to below 3% of gross domestic product (GDP), the reference value set out in the treaty.

As a result, whereas in May 2005 a majority of member states were subject to excessive deficit procedures, only two procedures now stay open. With Italy and Portugal lowering their deficits, none of the euro area's 15 member states remain in excessive deficit.

In the case of Slovakia, closure of the excessive deficit procedure is a necessary precondition for its adoption of the euro on 1 January next year, as proposed by the Commission.

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1 The decisions were taken by the Economic and Financial Affairs Council, meeting in Luxembourg.

Czech Republic

The excessive deficit procedure with regard to the Czech Republic was opened following a government deficit in 2003 that amounted to 12.9% of GDP (5.9% if a major one-off operation related to state guarantees is excluded). In July 2004, a few weeks after the Czech Republic's accession to the EU, the Council adopted a decision under article 104(6) on the existence of an excessive deficit, and a recommendation under article 104(7) setting out measures needed in order to bring the deficit below the EU's 3% reference value by 2008 at the latest.

It set deficit targets of 5.3% of GDP for 2004, 4.7% for 2005, 3.8% for 2006 and 3.3% for 2007. Special circumstances – especially the structural shift in the Czech economy following the country's accession to the EU – allowed for correction of the deficit not in the short term but in the medium term.

In January 2005, the Council concurred with a Commission assessment that the Czech Republic had so far taken effective action regarding measures to achieve the deficit target for 2005. In 2006, the Czech Republic reduced its deficit to 2.7% of GDP.

In March 2007 however, following elections the previous June, the Czech Republic announced new deficit projections of 4% of GDP for 2007, 3.5% for 2008 and 3.2% for 2009, thus missing the 3% threshold not only in 2008, but also in 2009. In July 2007, the Council therefore adopted a decision, under article 104(8) of the treaty, establishing that action taken by the Czech Republic was proving inadequate for bringing its deficit below the 3% threshold.

Given that the Czech Republic is not a member of the euro zone, the steps of the excessive deficit procedure provided for by article 104(9) and 104(11) do not apply. So in October 2007, the Council issued a new recommendation under article 104(7), calling on the Czech Republic to contain the budgetary slippage in 2007 and confirming 2008 as the target year for bringing its deficit below 3% of GDP.

To this end, it recommended an improvement in the cyclically-adjusted deficit (excluding one-off and other temporary measures) of at least 0.75% in 2008 compared with 2007, and set a deadline of 9 April 2008 for taking effective action.

In 2007, despite an expected fiscal expansion, the Czech Republic reduced its deficit to 1.6% of GDP, thanks to expenditure savings as well as strong growth. The cyclically-adjusted balance improved by 0.5% of GDP, while the Czech government introduced a range of measures aimed at consolidating public finances in 2008 and 2009.

The Council concluded that the Czech Republic's deficit has been brought below the 3% of GDP threshold in a credible and sustainable manner.

Italy

The excessive deficit procedure with regard to Italy was opened in July 2005, following government deficits of 3.5% of GDP in both 2003 and 2004. The Council adopted a decision under article 104(6) on the existence of an excessive deficit, and a recommendation under article 104(7) setting out measures needed in order to bring the deficit below the EU's 3% reference value by 2007 at the latest.

These included a 1.6% of GDP reduction in Italy's cyclically-adjusted deficit (excluding one-off and other temporary measures) over the 2006-07 period compared with 2005, as well as further fiscal consolidation in subsequent years and restoration of Italy's debt ratio to a declining path.

The deficit increased to 4.2% of GDP in 2005, before declining to 3.4% in 2006 and 1.9% in 2007, with the cyclically-adjusted balance improving by 3% of GDP over the 2006-07 period, well above the fiscal effort recommended by the Council.

As regards Italy's debt, after declining for a decade to just below 104% of GDP, in 2004 it remained well above the EU's 60% of GDP reference value for debt. It increased by 2% in 2005 and by a further 0.6% in 2006, before falling again to 104% in 2007.

The Council concluded that Italy's deficit has been brought below the 3% of GDP threshold in a credible and sustainable manner, and that, while its debt ratio remains high and clearly above the reference value, it can be considered to have diminished in line with the correction of its deficit.

Portugal

The excessive deficit procedure was opened in September 2005, after Portugal announced a projected government deficit amounting to 6.2% of GDP in 2005, with plans to bring the deficit below 3% of GDP no sooner than 2008. Government debt would remain in excess of the 60% of GDP reference value for debt, and continue rising until 2007.

The Council adopted a decision under article 104(6) on the existence of an excessive deficit, and a recommendation under article 104(7) setting out measures needed in order to bring the deficit below the EU's 3% threshold by 2008 at the latest. It called for a 1.6% of GDP reduction in Portugal's cyclically-adjusted deficit (excluding one-off and other temporary measures) in 2006 compared with 2005, to be followed by a further decrease of 0.75% of GDP in each of the two subsequent years.

The deficit declined to 3.9% of GDP in 2006 and to 2.6% in 2007, with a 2% of GDP improvement in the cyclically-adjusted balance in 2006 and a further 1% in 2007, well above the fiscal effort recommended by the Council.

The Council concluded that Portugal's deficit has been brought below the 3% of GDP threshold in a credible and sustainable manner.

Slovakia

The excessive deficit procedure with regard to Slovakia was opened following a government deficit in 2003 that amounted to 3.6%, according to data available at the time. In July 2004, a few weeks after Slovakia's accession to the EU, the Council adopted a decision under article 104(6) on the existence of an excessive deficit, and a recommendation under article 104(7) setting out measures needed in order to bring the deficit below the EU's 3% reference value by 2007 at the latest.

It set deficit targets of 4% of GDP for 2004, 3.9% for 2005, 3.9% for 2006 and 3% for 2007. Special circumstances – especially the structural shift in Slovakia's economy following its accession to the EU – allowed for correction of the deficit not in the short term but in the medium term.

According to Eurostat, in the light of revised data notified by Slovakia in April 2007, its deficit in fact remained below 3% of GDP during the 2003-05 period. But the headline deficit increased to 3.6% in 2006 before falling to 2.2% in 2007.

The Council concluded that Slovakia's deficit has been brought below the 3% of GDP threshold in a credible and sustainable manner.

Closure of the excessive deficit procedure is a necessary precondition for Slovakia's adoption of the euro on 1 January next year, as proposed by the Commission.