Public finances: contribution to growth and employment

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PURPOSE : to evaluate the contribution of public finances to the growth and employment. CONTENT : The Lisbon European Council of 23-24 March 2000 requested the Council and the Commission to present a report to the Spring 2001 European Council assessing the contribution of public finances to growth and employment, and on the basis of comparable data and indicators, whether adequate concrete measures are being taken in order to: - alleviate the tax pressure on labour and especially on the relatively unskilled and low-paid, improve the employment and training incentive effects of tax and benefit systems; - redirect public expenditure towards increasing the relative importance of capital accumulation · both physical and human · and support research and development, innovation and information technologies; - ensure the long-term sustainability of public finances, examining the different dimensions involved, including the impact of ageing populations, in the light of the report to be prepared by the High Level Working Party on Social Protection. The ECOFIN Council examined a progress report 1 at their meeting of 7 November 2000, which they considered to be a good basis for the Commission-Council report to be presented to the Stockholm European Council. The assessment of the impact of public finances on growth and employment is not straightforward. Governments pursue many policy objectives (to improve resource allocation, redistribution, stabilisation) through a variety of policy instruments regulation,spending, taxes), which inevitably means that the impact of public finances on the real economy is multiple and complex. The document underlines the need to maintain sound public finances in the third phase of EMU and examines if the recent budgetary developments indicate that the EU is on the right track. The report also studies the recent employment-friendly tax and benefit systems. Furthermore, the reform effort has been unequal with a comprehensive approach to reform of the tax system in some countries contrasting with a piecemeal approach in others. Many countries have taken steps to reduce taxes, notably employer's social security contributions, and more recently personal income taxes especially at the lower end of the earnings scale. The document examines the role of public finances for a knowledge-driven economy. Assessing the contribution of public finances to a knowledge-driven economy is timely given the ongoing debate on the 'new economy'. However, there are considerable difficulties making cross-country comparisons on public expenditures as there is a lack of data on both inputs by the public sector (i.e. a comparable functional classification of spending) or outputs (the efficiency and economic benefits of such expenditures). taxes. Greater efforts are needed to increase the investment necessary to facilitate the development of the information society Governments mustalso put more emphasis on education and training in order to equip European citizens with the necessary skills for an information society, while promoting the involvement of the private sector on innovation and R&D activities. Furthermore, restructuring of public spending should be complemented by institutional and structural reforms that enhance the role of market mechanisms and introduce adequate incentive systems to promote private accumulation of physical and human capital. Lastly, the report examines the long-term sustainability of public finances with regard to the impact of the ageing population which will lead to substantial pressure for increased spending on public pensions.