ILO Research Paper No. 7

International
Labour
Office

Macroeconomic policy advice and the Article IV consultations:

Comparative overview of the European Union member states

Mark Weisbrot
Helene Jorgensen

August 2013

ILO Research Paper No. 7

Macroeconomic policy advice and the Article IV consultations: Comparative overview of European Union member states

Mark Weisbrot
Helene Jorgensen

August 2013
International Labour Office

* Mark Weisbrot is an economist and Co-Director, and Helene Jorgensen is a Senior Research Associate at the Center for Economic and Policy Research, Washington, DC.

ISSN 2306-0875 (web pdf)

ILO publication and electronic products can be obtained through major booksellers or ILO local offices in many countries, or direct from ILO Publications, International Labour Office, P.O. Box 6, CH-1211 Geneva 22 (Switzerland). Catalogues or lists of new publications are available free of charge from the above address, or by email: pubvente@ilo.org. Visit our site: http://www.ilo.org/pubins

Table of contents

Acknowledgements

The authors would like to thank the following people for helpful reviews and comments: Prakash Loungani, Economist from the European Department of the International Monetary Fund, Peter Bakvis, Davide Furceri, Dean Baker, Anis Chowdhury, Dianne Holland, David Kucera, Simon Wren-Lewis, and Uma Rani. The paper was edited and updated by Iyanatul Islam. The authors also thank the International Labour Organization for their funding and support for this project. The standard disclaimers apply: errors and omissions, if any, represent the sole responsibility of the authors, while the views expressed here should also be attributed to them, and not to any other individual or organization. A longer version of this paper was released by CEPR in January 2012 and includes country-specific summaries which is available at:
http://www.cepr.net/index.php/publications/reports/macroeconomic-policy-advice-and-the-article-iv-consultations

Abstract

This paper examines 67 IMF Article IV consultations in 27 EU member states between 2008 and 2011, and shows that there is an overwhelming emphasis on fiscal consolidation, reduction of social expenditures, and measures that weaken the bargaining power and income of labour, and make it difficult to promote growth and employment. These findings are very similar to that brought out earlier for 50 low and middle-income countries. The review of Article IV agreements supports the view that policy mistakes by the European authorities, including IMFs priority of fiscal consolidation, have 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 paper suggests that IMF might wish to engage in Independent Evaluation Office review of its policy advice in Europe. The paper finally notes that there have been some important changes in 2012 and 2013, wherein IMF is engaging seriously with some of the deficiencies in Article IVs.

Keywords: macroeconomic policy formation, stabilization

JEL classification: E6

1 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 per cent for 2012 (as compared with 3.8 per cent for 2011 and 5.1 per cent 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, pp. 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; it 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" (2013a, p.2).

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.

Public access to Article IV consultations is of comparatively recent origin. It emanates from a pilot project that the IMF initiated in April 1999 to improve its transparency.[1] These consultations are a solid source of information on the nature of macroeconomic policy advice offered by the IMF to member states. Yet, unlike the extensive - albeit contentious - literature on the nature and impact of conditionalities that are enunciated under the IMF's lending arrangements, relatively little effort has been invested in undertaking a 'content analysis' of staff reports that support the Article IV

[1] See http://www.imf.org/external/pubs/pilot.htm

consultations in order to decipher the nature of the macroeconomic policy advice that is offered to member states.[2]

This paper intends to deal with such a lacuna by undertaking a content analysis of the policy advice given by the IMF to European Union countries in 67 Article IV agreements for the four years 2008-2011 (IMF, 2012b). 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 (i) 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 (ii) 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 global crisis. Instead of a multiplier of 0.5, they find a range of 0.9 to 1.7 (2012a, pp. 41-43). This could explain some of the large gap between the IMF's growth

[2] For a meta-analysis of studies that assess the impact of IMF conditionalities, see Steinwand and Stone (2008). As noted, the literature on the content analysis of Article IV consultations is relatively scarce. Two good examples are Momani (2006) focusing on Canada and Fratzscher and Reynaud (2011) focusing on 36 emerging economies. It is to be noted that, unlike in this paper, Fratzscher and Reynaud uses the PINs rather than the full staff reports.

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 per cent for 2011 and 1.1 per cent for 2012. The actual results were -6.9 per cent for 2011 and -6 per cent (October WEO projection) for 2012 (Weisbrot and Montecino, 2012). Similarly, in Latvia the IMF projected, in January of 2009, -5 per cent growth for 2009; the actual decline was 18 per cent (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 in June 2012 (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 global crisis, 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.[3]

[3] 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

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 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 [4] 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).[5] 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. The paper is structured as follows. Section 2 provides a brief description of methodology highlighting how the various country-specific reports were converted into comparable data pertaining to fiscal adjustment, inflation targeting, labour market policies and social policies. This sets the basis for a comparative overview of 67 IMF Article IVs for 27 EU member states spanning four years (2008-2011) in Section 3. Section 4 provides some insights into the Europe 2020 strategy and Article IV recommendations. Article IV recommendations and the business cycle are analyzed briefly in Section 5. Section 6 summarizes the key findings and notes that in the 2013 Jobs and Growth Report (released in March), the IMF has engaged – perhaps for the first time – in its own internal evaluation of Article IV consultations.

---

full 8.7 per cent of GDP during 2010-2011, with more tightening for 2012 and beyond, and the economy still shrinking.

4 "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." (Jones and Suoninen, 2012)

5 "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." (Fontanella-Khan, 2012)

2 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 recommendation, the third step linked the recommendation to a quote from the relevant Article IV consultation. In the final step, a review of the quotes was conducted to assess whether they were taken in or out of context.

2.1 Fiscal adjustment

The IMF Article IV consultations with EU countries typically center 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

2.2 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 per cent target"	Hungary 2008: 3
Interest rates	"further gradual hikes in the policy rate… would bring inflation back to the 2½ per cent 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

2.3 Labor market policies

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

2.4 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.

Table 5: Real GDP growth (annual per cent 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.

3 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. It does not seek to offer long-term analysis of alternative policies.

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, “historical experience indicates that successful fiscal consolidations were often launched in the midst of economic downturns or the early stages of recovery”[6] (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 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, “although this consolidation effort involves painful decisions and dampens short-run growth, it is necessary to enhance credibility and ensure fiscal sustainability” (p. 26).

3.1 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). [7]

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, “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

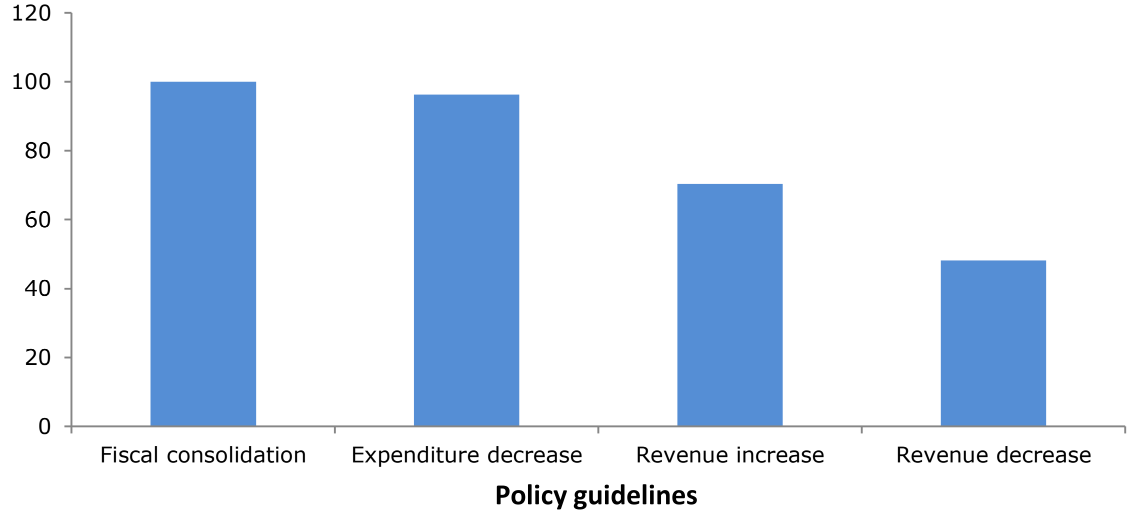
[6] The IMF report did not provide a reference for this claim. Here, it is worth citing that the IMF’s research argues the opposite, that is, fiscal consolidation is best undertaken during normal periods of growth and that consolidation exercises should be carefully sequenced. Perhaps this is the reason 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).

[7] The IMF did not provide a reference for this claim in any of the reports mentioned.

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 per cent). 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 per cent of countries. On the other hand, revenue increases were recommended in 70.4 per cent 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 per cent of the countries.

Figure 1: Country frequency of fiscal policy recommendations for EU countries, 2008-2011 (in per cent)



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

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). 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" [8] (p. 28).

[8] No references were provided. See above.

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 per cent is commendable" (p. 16). IMF staff found "the current fiscal rules -- targeting a surplus of 1 per cent of GDP across the cycle, supported by medium-term expenditure ceilings – remain[ed] well suited for Sweden" in the 2010 consultation (2010, p.36). Few consultations reviewed expressed concerns about planned fiscal consolidation. The consultation with Poland warned that "aiming at a deficit of 3 per cent 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 government debt is likely to remain sustainable, fiscal consolidation is necessary in light of the uncertainty in financial markets and contingent liabilities" (p. 8).

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

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

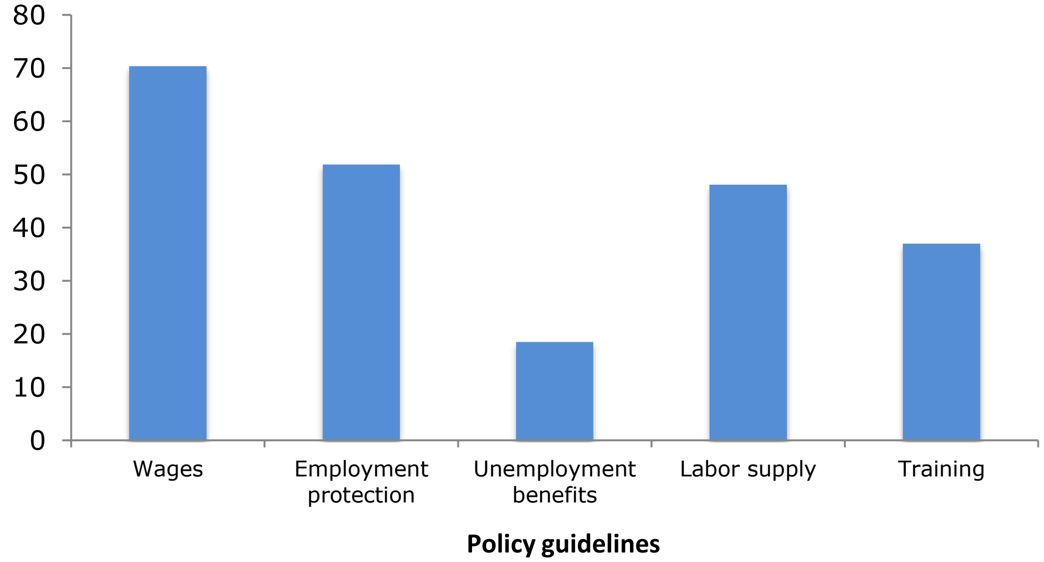
3.2 Inflation targeting

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).

3.3 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 per cent in Austria to 20.1 per cent in Spain (see Table 7).

Figure 2: Country frequency of labor market policy recommendations for EU countries, 2008-2011 (in per cent)



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

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 for 48.1 per cent of countries. In every case, the advice promoted policies increasing labor supply. Finally, IMF recommended scaling back employment protections in all the 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.

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, 2008-11 [9]

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	

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.

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.

[9] It is not being implied that there is a direct correlation or causality between the demographic measures and policy recommendations, but that recommendations should be anchored in the reality of the demographics. For example, it is striking that the IMF recommends increasing labour supply for Denmark that has one of the highest employment to-population ratios in the world; or recommends increasing the retirement age regardless of life expectancy.

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" [10] (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.

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).

The labor force participation rate varied widely across EU countries, with Malta (60.3 per cent), Italy (62.2 per cent) and Hungary (62.4 per cent) having the lowest rates and Denmark having the highest rate (79.4 per cent) (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 discuss 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.[11] 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.

[10] The 2009 consultation with Cyprus proposed flexicurity as an option in the public sector.

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

3.4 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 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).

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).

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

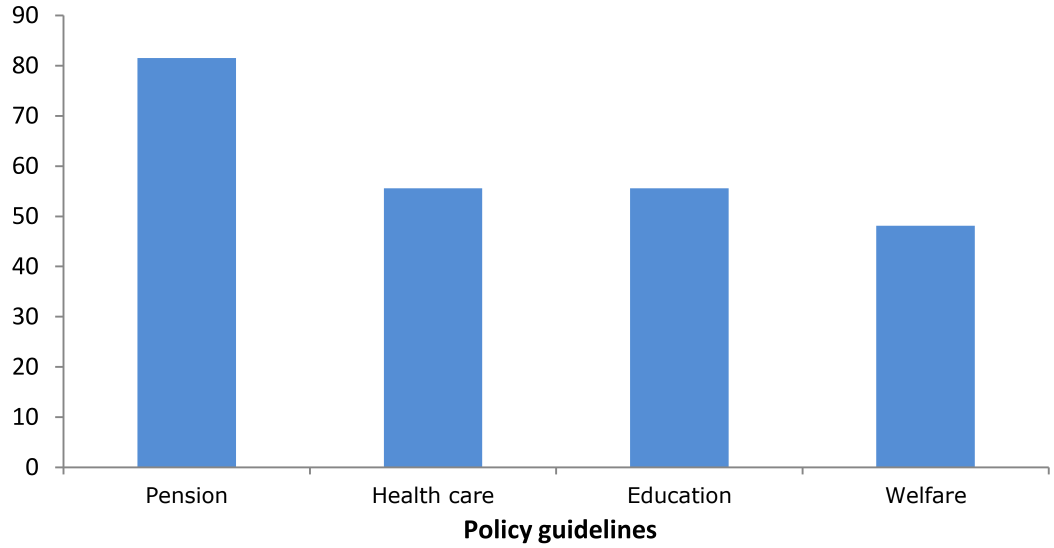
Note: “1” denotes a recommended increase or expansion of policy, “2” denotes a recommended decrease or contraction of policy; and “N” denotes either neutral or could not be determined from the information provided.
Source: World Bank, Data Indicator, Life expectancy at birth, total (years); and various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

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, p.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: Country frequency of social policy recommendations for EU countries, 2008-2011 (in per cent)

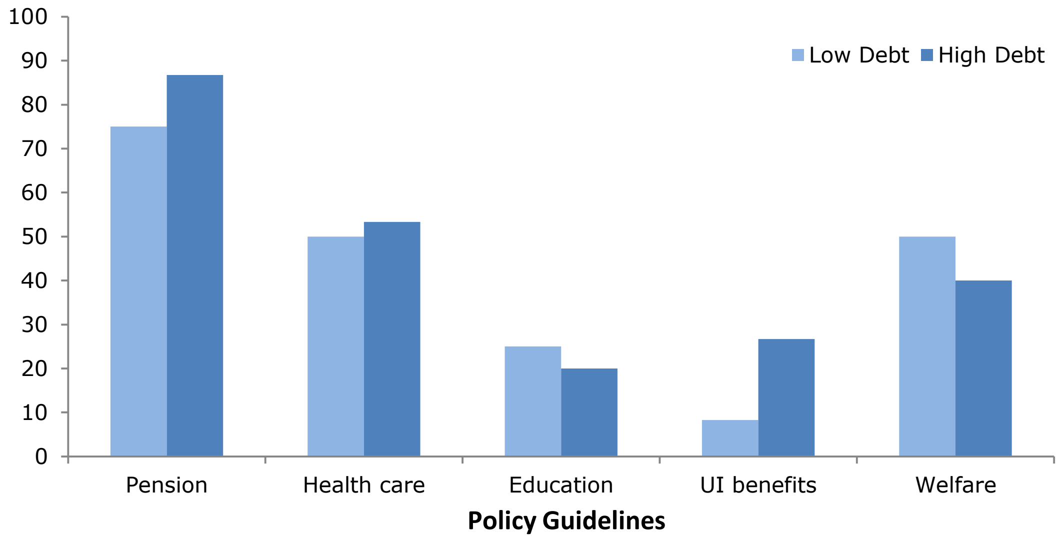


Note: Education variable does not include advice on apprenticeship and training programs.
Source: Various Article IV consultation reports with EU countries, 2008-2011.

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 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 per cent of GDP (2008-2011) were categorized as low debt, and fifteen countries with an average gross debt of 50 per cent 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 %)



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

4 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, research and development, 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: i) digital agenda; ii) innovation union to support research and development; iii) increase youth employment; iv) resource efficiency; v) industrial policy for the globalization era; vi) agenda for new skills and jobs; and vii) European platform against poverty.

The Europe 2020 Strategy provides few specifics on reaching the identified goals. For example, the concrete actions described for New Skills and Jobs Agenda 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 per cent for EU, with Denmark and the Netherlands having the most ambitious targets of 80 per cent 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).

5 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 per cent in 2011, and was projected to decline by an additional 6.0 per cent in 2012 (IMF 2012a, Table A2). The 2008 consultation with Italy projected output "to contract by about ½ per cent in 2008 and 1 per cent in 2009" (p. 3). In 2009, Italy's real GDP declined by 5.5 per cent, 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 per cent 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 per cent 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 per cent, 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 per cent 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).

6 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 signalling 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, 2012b, Table 2a; IMF, 2012c, Table 3a). It should be noted that the European governments who sit on its Board of Governors and Executive Board, and especially the larger countries overwhelmingly influence the IMF's decisions and recommendations in Europe. 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. Nonetheless, the IMF is by virtue of its lending 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 per cent 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 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: pp. 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.

Finally, it is worth reporting here that there have been some important changes in 2012 and 2013 that suggest that the IMF is indeed beginning to engage more seriously with some of the deficiencies in the Article IVs that have been documented in this paper. To start with, templates on employment projections that can be included in the Article IVs have been developed and are already in use (IMF, 2012d). The IMF has also undertaken its own content analysis of Article IVs – perhaps the first time that it has done so in a systematic manner. In its overarching Jobs and Growth report (IMF, 2013b), there is a brief section dedicated to 30 Article IVs spread across advanced economies (8), emerging economies (12) and low income economies (10). The evaluation concludes that the approach taken in bilateral surveillance is to recommend policies that are 'best suited to bringing about or maintaining macroeconomic stability' (IMF, 2013, p.34). The evaluation finds that the discussion of labour market issues 'appear limited', while '…enhancing (labour market) flexibility is a frequent theme…' (IMF, ibid, p.35). The evaluation is candid in noting that there is '…only a limited discussion of efficiency-equity trade-offs and there is little apparent tailoring of policies to country preferences…'(IMF, ibid, p.35). In other words, the 'one-size-fits-all' nature of the Article IVs highlighted in this paper is indeed valid.

The Jobs and Growth Report then proceeds to recommend that in its country and policy work the Fund should focus a lot more on analytical work on the determinants of inclusive growth and that advice on labour market policies should include collaborative work with other international institutions, most notably the World Bank, the OECD and the ILO. The expectation of the international community is that these recommendations will, over time, be consistently implemented.

References

Barroso, J.M.D. 2012. *Towards Europe 2020: Building a foundation for future prosperity*, speech delivered at The Europe 2020 Summit of the Lisbon Council, Brussels, 27 Feb.

Batini, N.; Callegari, G.; Melina, G. 2012. *Successful austerity in the United States, Europe and Japan,* IMF Working Paper WP/12/90 (Washington, DC, International Monetary Fund (IMF)).

Barkbu, B.; Rahman, J.; Valdés, R. 2012. *Fostering growth in Europe now*, IMF Staff Discussion Note SDN/12/07 (Washington, DC, International Monetary Fund (IMF)).

European Commission. (2012a). *Europe 2020: Europe's growth strategy* October. http://ec.europa.eu/europe2020/index_en.htm

—. (2012b). *European platform against poverty*. http://ec.europa.eu/social/main.jsp?langId=en&catId=961

Fontanella-Kahn, J. 2012. *European unemployment remains at high*, Financial Times, October 1, http://www.ft.com/cms/s/0/8d3d76c6-0bb3-11e2-b8d8-00144feabdc0.html#axzz2adFCFuAd

Fratzscher, M.; Reynaud, J. 2011. "IMF surveillance and financial markets: A political economy analysis", in *European Journal of Political Economy*, Vol. 27, No. 3, pp. 405–422.

Independent Evaluation Office. 2011. *IMF Performance in the run-up to the financial and economic crisis: IMF surveillance in 2004–07* (Washington, DC, International Monetary Fund (IMF)).

International Monetary Fund (IMF). 2011. *2011 Triennial Surveillance Review*, available at: http://www.imf.org/external/np/spr/triennial/

—. (2012a). *World Economic Outlook: Coping with high debt and sluggish growth* (Washington, DC).

—. (2012b). *IMF Financial Activities: Update November 12, 2009*.

—. (2012c). *IMF Financial Activities: Update November 15, 2012.*

—. (2012d). *A template for analyzing and projecting labor market indicators*, Middle East and Central Asia Department (Washington, DC).

—. (2007-2012). *Various Article IV Staff Reports.*

—. (2013a). *Factsheet: IMF Surveillance*, available at: https://www.imf.org/external/np/exr/facts/surv.htm

—. (2013b). *Jobs and growth: Analytical and operational considerations for the fund* (Washington, DC).

Islam, I.; Ishraq, A.; Rathin, R.; Ramos, R. 2012. *Macroeconomic policy advice and the Article IV consultations: A development perspective,* ILO Research Paper Series No.2 (Geneva, ILO).

Krugman, P. 2012. *End this depression now!* (New York, NY, W.W. Norton & Company).

Momani, B. 2006. “Assessing the Utility of, and Measuring Learning from, Canada’s IMF Article IV Consultations”, in *Canadian Journal of Political Science*, Vol. 39, No. 2, pp. 249–269.

Steinwand, M.; Stone, R.W. 2008. ‘The International Monetary Fund: A review of the recent evidence”, in *The Review of International Organizations*, Vol. 3, No. 2, pp. 123–149.

Weisbrot, M.; Åslund, A. 2012. *Latvia’s recession and recovery: Are there lessons for the Eurozone?*, panel held at the Center for Economic Policy Research, Washington, DC, 11 April.

—; Ray, R.; Johnston, J.; Cordero, J.A.; Montecino, J.A. 2009. *IMF-supported macroeconomic policies and the world recession: A look at 41 borrowing countries*, CEPR Reports and Issue Briefs 2009-37 (Washington, DC, Center for Economic and Policy Research)

—; —. 2010. *Latvia’s recession: The cost of adjustment with an internal devaluation*, CEPR Reports and Issue Briefs 2010-02 (Washington, DC, Center for Economic and Policy Research).

—; —. 2011. *Latvia’s internal devaluation: A success story?*, CEPR Reports and Issue Briefs 2011-25 (Washington, DC, Center for Economic and Policy Research).

—; Montecino, J. 2012. *More pain, no gain for Greece: Is the Euro worth the costs of pro-cyclical fiscal policy and internal devaluation?*, CEPR Reports and Issue Briefs 2012-07 (Washington, DC, Center for Economic and Policy Research).

Appendix

Table 1: 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