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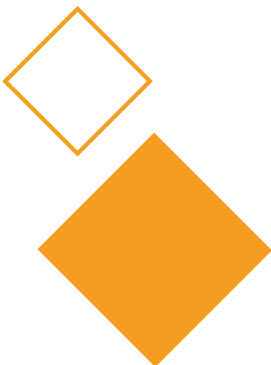

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INEQUALITIES IN THE EUROPEAN SEMESTER

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FOREWORD

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In the last decade, the economic architecture of the European Union has faced major challenges and had to adapt fast to provide sound responses and remedies to several crises that undercut the income and the security of many Europeans. Introduced exactly a decade ago, the European Semester process soon became the pivotal tool for economic coordination in Europe and in essence it epitomizes the way to steer an economic doctrine across the EU, from the Commission and the Council to national governments and budgets.

Initially anchored to the jointly agreed targets of the Europe 2020 Strategy, it soon abandoned the shared goals to focus on the priorities set by the first „political” Commission. It has been used, at least for the first few years, almost uniquely to serve the objective of fiscal consolidation. There is no need here to stress how much that has compromised the ability of the European public sector to counteract the different socio-economic emergencies and fuelled disaffection to the European project and to politics.

Indeed, the Semester has evolved and thanks to the political agenda and Social Scoreboard enshrined in the European Pillar of Social Rights, we have started to see Country Specific Recommendations promoting social investment and social dialogue. Finally, green and climate concerns have become more

central, for an Annual Growth Survey that now addresses Sustainability as the backbone of a Growth Strategy.

That is however not enough, particularly in view of the dire consequences of the pandemic. With a total estimated loss of 13% of working hours in Europe and 20% of youth out of work due to COVID-19 (see [ILO Monitor](#)), with as much as 6 million people newly unemployed (see [Eurostat NewsRelease](#)), European Institutions need to go beyond the provision of funds. The Next Generation EU and SURE are good novelties but we must dare to change the economic paradigm once for all. So that forward-looking investment, protection of incomes and quality in public services, such as health, are not the immediate response to a crisis but the norm. The goal of the European public sector.

As its history undoubtedly shows, the EU is able to be a beacon of wellbeing and prosperity for this continent and its leaders should live up to these expectations. In this respect, the European Semester is the focal policy in which such a new course shall be established.

In line with the European Parliament [Report on Combating Inequalities as a lever to boost job creation and growth](#) we also believe that „inequalities threaten the future of the European project, erode its legitimacy and can damage trust in the EU as an engine of social progress”.

All too often, Europe has prioritised macro-economic stability and failed to understand that social stability and cohesion are essential for the political and economic stability that can deliver on macroeconomic soundness. It is no longer possible to ignore the distributional effects of macroeconomic policy and EU recommendations.

There is by now overwhelming evidence that socio-economic well-being is a prerequisite for sustainable and inclusive growth and political stability. We have learned to admit that too much inequality is bad for growth; it is now time to go one step further and recognise that equality is the foundation of the type of growth we want for Europe and for the Europeans.

It is no surprise that the Covid-19 outbreak has not affected countries and communities evenly. The pandemic, as well as its economic consequences, jeopardise vulnerable groups and people experiencing poverty and social exclusion to. A special effort is necessary if we do not want to see Europe emerging from this crisis more unequal than before.

To this end we recommend a strong refocusing of the European Semester toward the fight against inequality; for a healthier society that delivers healthier economic outcomes.

As the Study by Antonucci & Corti points out, the very first step should be to elaborate a working definition of what inequality is with respect to EU internal policies. Much has been said about aligning EU policy action to the Sustainable Development Goals but very limited steps have been taken to operationalise the SDGs within Europe. This study on Inequality and the European Semester offers an operational definition of inequality that could and should serve as a prism to rethink the European Semester.

The first consequence of this new approach would be to revise the indicators of the Semester to correctly monitor inequality. This would imply considering indicators of precarity, job and financial insecurity, and access to opportunities – such as childcare and social or health services.

A second consequence would be to start using the European Semester framework to steer the other side of national public finances, not the expenditure, but the revenue side. Country-specific recommendations do not focus on tax issues often; when they do so, it is mostly to promote efficiency in labour markets with a rather ambiguous invitation to „a reconfiguration of the taxation mix”. Personal income taxation, corporate taxation, wealth and inheritance taxes and environmental taxes are instead central mechanisms to address inequality and secure opportunities for all.

As the authors explain, by expanding the focus from poverty to inequality, from the bottom of the income distribution to the whole distribution of incomes and opportunities, our Union would be better equipped to address the sharp decline in socio-economic conditions that the European middle class is facing.

The economic governance of the European Union has changed fast to adapt to the unexpected pandemic and its effects; now, a serious reflection has to be done to re-define the goals of the interventionism and coordination carried out by the EU via the European Semester. If we are serious about leaving to the next generation of Europeans a more sustainable, socially equitable and economically stronger Union, a full-fledged strategy to fight inequalities is the way to go.

EXECUTIVE SUMMARY

With the launch of the European Pillar of Social Rights, the Commission has adopted a new ambitious social policy framework. The aim is to support fair and well-functioning labour markets and welfare systems, for a renewed process of upward convergence towards better working and living conditions in Europe. Despite fighting inequality figures as one of the prominent challenges the Social Pillar aims to tackle, the European Semester, the EU coordination mechanism of socio-economic policies, still lacks a comprehensive framework to monitor socio-economic inequalities within member states. We address these drawbacks and propose a new framework to tackle inequalities in the Semester.

In [Section 1](#) of this policy paper, we provide an ‘operational’ definition of inequality in the Semester, which serves as a ‘toolkit’ to assess the extent to which the country specific recommendations are ‘inequality proof’. We apply this operational definition to examine three main policy areas: 1) social and employment policies [[Section 1.1](#)]; 2) public finance and economic policies [[Section 1.2](#)]; and 3) taxation policies (including labour, corporate and capital income taxes, taxes on immovable

property, net wealth and inheritance taxes, VAT and environmental taxes) [[Section 1.3](#)].

For each policy area, the paper offers an assessment of the relevance and the capacity of the indicators currently used by the European Commission, to account for the inequality dimension in the three policy areas identified above. Based on the definition provided above, the paper provides an analysis of the country-specific recommendations addressed to member states in 2019, with the aim of understanding the distributional impact of the policy reforms based on the current set of indicators

With respect to traditional social and employment policies [[Section 2.1](#)], we show that the attention remains on measuring disadvantage at the bottom of the income distribution, with most of the indicators and of the recommendations focused on poverty and social exclusion, i.e. on individuals at the bottom of the income distribution. By contrast, no attention is paid to the declining condition of intermediate segments of the population (the so-called ‘squeezed middle’). Indicators on job insecurity, financial insecurity and job tenure insecurity,

RECOMMENDATIONS ADDRESSING INEQUALITIES

Policy interventions that address the effects of the socio-economic polarisation of the society (the declining position of the middle class) both directly (through explicit social policy mechanisms) and indirectly (through the effect of economic policies on the social sphere & considering the net effect of taxation)

Socio-economic issues beyond poverty and social exclusion

Feedback loop between the ‘economic’ and the ‘social’

The net balance between ‘paying in’ and ‘getting the rewards’

which interest an increasing portion of individuals living in Europe, are missing. Finally, the focus on inequality of opportunities is missing in social investment areas, such as childcare and the accessibility of social services.

Concerning the macroeconomic recommendations [Section 2.2], our analysis reveals a persisting focus on budgetary stability and debt reduction, in particular in health and pension, which might have a regressive effect on overall inequality, as well as a limited focus on public investment. The current Macroeconomic Imbalance Procedure (MIP) scoreboard is devoid of macroeconomic indicators that take into account the inequality dimension. Regarding the country specific recommendations, we highlight that, even though the macroeconomic framework defined in the Semester does not ask for explicit cuts and reductions in public expenditure, it indirectly affects member states' capacity to use public resources to redistribute and conduct public investments, by setting tight constraints and setting the limits of governments' initiative.

Finally, with respect to taxation policies [Section 2.3], we show that the indicators used by the Commission are adequate to the progressivity of the taxation system. However, our analysis shows that the attention of the country specific recommendations to the progressivity of personal income taxation is primarily oriented toward the efficiency and productivity of the labour market, rather than toward redistributing resources (especially on middle and lower-middle groups). Most of the recommendations do not have an explicit focus on progressive taxation, proposing a non-defined 'reconfiguration of the taxation mix'. In addition, we show inconsistencies between the problems identified in the country reports (e.g. inheritance and high-income taxation), and the actual content of the countryspecific recommendations.

In order to address the shortcomings identified above, we propose nine recommendations on how the Semester can effectively monitor and address inequalities.

RECOMMENDATION GROUP 1



Integrate the focus on social exclusion by considering the rising socio-economic insecurity affecting the majority of the population, in particular the declining lower-middle class in Europe

RECOMMENDATION GROUP 2



Consider the redistributive effects of economic policies by creating a bridge between the economic and the social aspects

RECOMMENDATION GROUP 3



Link the spending and funding sides of the redistribution mechanisms by considering the redistributive effects of taxation

In the first group of recommendations (no. 1-2-3), we propose to include new indicators in the Semester in order to: a) capture the declining quality of work among the majority of workers (job-status insecurity, job quality and work representation); b) assess households' financial capability and financial fragility; and c) measure income and wealth inequality pre and post taxes.

In the second group of recommendations (no. 4-5-6), we propose to: a) integrate new auxiliary indicators in the MIP to monitor household financial fragility; b) revise the EU fiscal framework and especially the expenditure rules of

the Stability and Growth Pact; c) involve the social actors in a formalised way in the drafting process of the macroeconomic recommendations.

Finally, as concerns the third groups of recommendations (no. 7-8-9), we recommend: a) an expansion and consistent use of progressive taxation recommendations that are currently made only for countries with very regressive taxation arrangements; b) a coordinated approach to EU tax erosion and taxation dumping; and c) expand the tax base using new areas (e.g. environmental taxation) in a progressive way.

INTRODUCTION

Since its inception, the European Semester has attracted interest in the effects of its recommendations –country-specific recommendations (CSRs) and annual growth surveys (AGSs) – on the EU’s social outcomes. Recently, a number of political initiatives have proposed using the European Semester as a mechanism to reduce inequalities (see the European Parliament resolution of 16 November 2017 on ‘Combating inequalities as a lever to boost job creation and growth’).

This policy paper proposes a new framework to address inequalities through the European Semester by considering three elements that are currently overlooked in the way the European Semester is framed:

1. integrating the focus on social exclusion by considering the rising socio-economic insecurity affecting the majority of the population, in particular the declining lower-middle class in Europe;
2. considering the redistributive effects of economic policies by creating a bridge between the economic and the social aspects;
3. linking the spending and funding sides of the redistribution mechanisms by considering the redistributive effects of taxation.

Despite the divergence on the qualitative impact of the European Semester (Crespy and Menz, 2015 vs Zeitlin and Vanherke, 2018), scholars agree that the Semester is an instrument that has ‘hardened’ the policy influence of the EU on member states compared to pre-existing softer mechanisms, such as the open method of coordination (OMC) and, in some respects, the European Social Dialogue (de la Porte and Heins, 2014). In the context

of the current Covid-19 crisis, the Semester emerges as a potentially powerful instrument to steer member states’ national reforms, and especially after the adoption of the new Recovery and Resilience Facility within Next Generation EU. Indeed, the outbreak of the pandemic has resulted in an exacerbation of existing dynamics of inequality with a decline in job quality and a widespread diffusion of job tenure and job status insecurity; an emergence of ‘invisible’ forms of disadvantage (e.g. migrants, care workers and gig workers) (Forum on Inequality and Diversity, 2020); and, finally, a partial abandonment of previous macroeconomic paradigms that, as we see below, have a regressive effect on socio-economic inequality.

Our contribution will be framed in the following way: after a brief discussion of the context around our proposal, the first part will present an operational definition of addressing inequalities within the European Semester; the second part will offer an analysis of the European Semester and its recommendations through the lens of addressing socio-economic inequalities; the third part will propose nine recommendations in line with the new framework, including a new set of indicators.

The context: the shift towards inequality and the European Pillar of Social Rights

Since the mid-1990s, the social policy agenda of the EU, inspired by the social investment paradigm, has focused on human capital development and on targeting social provisions, spending around labour market outsiders and socially excluded individuals. In this framework, social protection has been a mechanism that acts to re-include/re-insert individuals in the labour market (Begg and Berghman, 2002: 185). The Europe 2020 strategy and, in particular, the adoption of the Social Invest-

ment Package (SIP) by the European Commission in 2013, emphasise the importance of human capital investment in order to make the labour market more flexible while having policies in place to include labour market outsiders (European Commission, 2013). As a consequence, in part, of EU pressure, from the late 1990s, European welfare states have engaged, with varying degrees and following different paths, in a progressive recalibration of their welfare state interventions toward social investment (e.g. training schemes; investment in human capital) (Vandenbroucke and Vleminckx, 2011; Nikolai, 2012; Vaalavuo, 2013; Hemerijck, 2013; van Vliet and Wang, 2015; Kuitto, 2016), even after the 2008 crisis (van Kersbergen et al, 2014; Kvist, 2013). In many member states the adoption of social investment policies has also been characterised by the concurrent reduction of direct cash redistribution – that is, all the types of cash support that citizens receive from social insurance and social assistance schemes – considered ‘passive’ social policy schemes (Marx, 2013).

In this context, the European Semester has, since its inception, largely promoted the shift towards the social investment paradigm. The first decade of the Semester’s recommendations on social investment were embedded in an agenda which prioritised restrictive macro-economic policy, labour mobility and flexible labour market policies that contributed to the creation of an environment that is highly unfavourable to direct universal cash redistribu-

tion measures. Although at the time of writing a significant re-orientation of the Semester’s recommendations has occurred in the field of social and employment policies, the Semester still remains devoid of a focus on inequality. This does not come as a surprise since the two narratives that accompanied the European social strategy between 2011 and 2017, namely Europe 2020 and the SIP, have an explicit focus on poverty, social exclusion and human capital investment.

The adoption of the European Pillar of Social Rights (EPSR) however, seems to have opened a window of opportunity for the EU to adopt a new fully fledged strategy to fight inequalities. Compared to the SIP, in fact, the EPSR includes some elements that move towards a more enlarged vision of social policy: improving the working conditions of labour market insiders; re-instating strong minimum-income universal safety net ‘buffers’; easing and improving the ‘flow’ of contemporary labour-market and (gendered) life-course transitions.¹ Furthermore, the EPSR partially overcomes the ‘social policy as mere productive factors’ approach which characterised the SIP, re-establishing a role for social policies independent from their contribution to economic objectives. The analyses of CSRs addressed to member states between 2018 and 2019 confirm an increased attention to social protection and inclusion, and especially a progressive abandonment of the previous approach to social policies based on labour and wage flexibilisation and collective bargain decentralisation that characterised the

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¹ The stock, buffer and flow taxonomy refers to a welfare state’s functions elaborated by Hemerijck (2013). The ‘flow’ function is about allocation of labour and employment over the lifespan, making sure that school-leavers, parents (especially mothers), unemployed workers, older workers or the disabled can return to work as fast as possible through active labour market policies, job-matching, work-life balance services and assistance during vulnerable transitions. The ‘buffer’ function is about securing adequate and inclusive income protection. A traditional example is unemployment insurance schemes. The ‘stock’ function refers to policies aimed at enchainning and maintaining human capital or capabilities over the life-course in an ageing society, by bringing under one roof adjustable bundles of professional assistance from childcare to elderly care, including skill enhancement and training services in case of unemployment, as well as health, family and housing support.

The immediate fiscal response put in place by member states to cushion the effects of the pandemic has directly called the EU fiscal framework into question, especially the expenditure rules.

first Semester cycles (Corti, 2020). As stressed by various authors (Galgóczi et al, 2017; Sabato et al, 2018), however, not all the principles of the Social Pillar have been translated into measurable indicators in the Semester, nor an explicit strategy to go beyond the Europe 2020 agenda and the SIP, with a consequent lack of an explicit take on inequality. Furthermore, as indicated by the ‘Social Sustainability’ report commissioned by the Employment and Social Affairs Committee in the European Parliament (McGuinn et al, 2020), the EPSR presents several limitations, such as the lack of targets set in the identified area and the partiality of the indicators used.

In this respect, the crisis caused by the outbreak of the Covid-19 pandemic seems to have opened a further window of opportunity for a revision of the Semester monitoring and recommendations. On the one hand, the socio-economic consequences of the current crisis have indeed emphasised the need to expand the coverage of social protection systems and to protect ample segments of the population (new groups as well as those traditionally considered at risk). On the other hand, the immediate fiscal response put in place by member states to cushion the effects of the pandemic has directly called the EU fiscal framework into question, especially the expenditure rules. In this respect, the high concentration of recommendations on extending the coverage of social security systems, activating automatic stabilisers, strengthening healthcare systems, re-establishing well-functioning social dialogue relationships and re-

skilling workers, all show a partial shift in focus in the Commission’s priorities (Rainone, 2020). At the same time, the activation of the general escape clause, which allows a temporary deviation from the member states’ budgetary medium-term objectives (MTOs) in order to tackle the pandemic, directly calls into question the governance of the EMU and opens margins of manoeuvre for a long-term revision of the fiscal framework.

With respect to fiscal policies, the Commission has stressed, even more than in the previous rounds, the importance of public investments. The Commission puts emphasis on ‘productive’ public expenditure for “stronger and more effective welfare states, active labour market policies and skills development” (European Commission, 2020c: 5), with the aim of ensuring the provision of essential services, of providing adequate income replacement, and of facilitating greater access to social protection. Despite the partial improvements of this last cycle, now the post-Covid-19 agenda also lacks some key elements to address inequality: it remains largely focussed on productive elements of social policy; it lacks an understanding of the economic-social nexus (i.e. considering the long-term macroeconomic implications of extending social protection in a macroeconomic framework that is only temporarily suspended); and it lacks an explicit focus on inequality (mentioned only for taxation) and on the redistributive effects of social policies. The agenda that we set out below to address inequality in the European Semester lays the framework to shift the focus in this direction further.

1. TOWARDS AN OPERATIONAL DEFINITION OF ADDRESSING INEQUALITIES WITHIN THE EUROPEAN SEMESTER

The topic of inequality has attracted a plethora of definitions. For the purpose of this policy paper, we employ an ‘operational’ definition of inequality that can be used for reforming the European Semester and that is attached to existing definitions. We define policies to address inequality in the framework of the European Semester in the following way:

Policy interventions that address the effects of the socio-economic polarisation of society (the declining position of the lower-middle segments of the population) both directly (through explicit social policy mechanisms) and indirectly (through the effect of economic policies on the social sphere). The indirect element considers the allocation of resources for redistribution by the state in order to have a net positive balance between taxation and social provisions both intra-generationally and inter-generationally.

This is a context-based definition of inequality that captures the emerging evidence of the declining position of individuals in the middle of the wealth and income distribution (Piketty, 2014; Milanovic, 2016) and considers how the European Semester intervenes both directly (through explicit social policies) and indirectly (through the effect of economic policies). Our definition takes into account both vertical inequalities (variations in outcomes among

individuals or households within each European member state) and horizontal inequalities (namely cross-national inequalities, using the core-periphery divide that is well established within the European Studies literature, see Antonucci and Varriale, 2020; Magone et al, 2016).

Our operational definition of addressing inequalities in the framework of the European Semester goes beyond the division between ‘economic’ and ‘social’ inequalities, to consider the mutual interaction between the two, namely the socio-economic aspect of inequalities. Within this framework, inequalities of outcomes in economic terms (namely the distribution of income, wealth etc) are deeply linked to inequalities of opportunities that tend to be framed in a ‘social way’ (access to education, risk of poverty etc). At the same time, inequalities of opportunities in labour market conditions have clear economic implications, given that they involve the relationship between workers and employers (so the economic interaction between labour and capital). Finally, our definition also refers to the renewed debate on the mechanisms of contributions and on how (through taxation of wealth and income) inter-generational and intra-generational inequalities can be addressed or reproduced through public policies (see Atkinson, 2014). Our framework to address inequalities in the Semester consists of three specific proposals:

1.1 ADDRESSING THE GROWING SOCIO-ECONOMIC INSECURITY IN EUROPEAN SOCIETIES BEYOND POVERTY AND SOCIAL EXCLUSION

As mentioned earlier, addressing social exclusion has been a popular paradigm in EU social policy. It was first established using the OMC (Begg and Berghman, 2002) and then integrated into the European Semester, at least in its ‘socialised’ version (Zeitlin and Vanherke, 2018). Quantitative targets for reducing poverty and social exclusion have been adopted by the Europe 2020 agenda (reduction of individuals affected by poverty and social exclusion to 20 million by 2020) and these targets have been incorporated into the European Semester, as the governance process of Europe 2020 (Copeland and Daly, 2018). Social exclusion and poverty are so central to the EU social policy framework that both positive (Jessoula, 2015; Zeitlin and Vanherke, 2018) and more sceptical (Copeland and Daly, 2018) analyses of the European Semester regard poverty and social exclusion as the backbone of European social policy.

Why should the EU expand its strategy to address socio-economic inequality?

The social inclusion paradigm was a product of a different social environment – that of the 1990s and 2000s – that had different employment rates and, above all, a much higher capacity of employment to lead to social integration. In particular, there has since been an increase in employment insecurity and ‘job tenure insecurity’, which is connected to the diffusion of short-term jobs or jobs with a fixed tenure. With the exception of Spain and Greece, the employment rates in Europe just before the onset of the Covid-19 crisis were higher than they were before the crisis of 2008. However, the quality and composition of the job market and working conditions are now extremely different. There has been an increasing share of temporary employment

contracts in the total jobs created within each country. The highest incidences of temporary contracts are in the Netherlands, Poland, Portugal, and Spain: between 21 and 27 per cent of the working age population (which is higher than the OECD average of 11.5 per cent) (ter Weel, 2018); temporary employment contracts have also sharply increased in France and Italy (ibid). Furthermore, as described by Gallie (2017), the 2008 crisis period transformed the quality of work, leading now to greater work intensity, less autonomy at work and a reconfiguration of the relationship between workers and employers. There is also a more hidden, and pernicious, form of insecurity concerning ordinary workers: job status insecurity, or the growing threat to working conditions of employed individuals. This refers to all aspects of work that can affect individuals in permanent jobs, such as declining benefits, sick-leave compensation, a worsening relationship with management, an unreasonable work–life balance, and so on. This ‘hidden form’ of employment insecurity is becoming highly prevalent in the workforce (Gallie et al, 2017).

In addition to this, we are witnessing the speedy development of a new grey area of labour market work, namely informal work, self-employment or gig economy work. Gig workers are workers who perform short on-demand ‘tasks’ for customers (the gigs), often through the mediation of digital platform businesses. Gig economy workers are generally classified as self-employed workers and, therefore, in addition to the labour market risks described above, they are also unable to access most labour protection mechanisms available to employed individuals (Colin and Palier, 2015). While the size of the gig economy is extremely difficult to calculate (Healy et al, 2017; Office of National Statistics, 2017), the first European-wide study estimates that this sector involves about 8-12 per cent of workers across Europe (Huws et al, 2017). As indicated by the report of the CLASS (Centre for Labour and Social Studies) think tank, the

The combined effect of employment insecurity and financial insecurity has affected not only labour market outsiders, but also labour market insiders.

Covid-19 crisis has affected (and will affect) in particular self-employed workers, workers in zero-hours contracts, agency workers and other casual workers (Shaheen and Jesse, 2020).

The increase of self-employment has contributed to overall income polarisation, as self-employed individuals are over-represented at the bottom and the top of the income distribution (Schneck, 2018). Adding insult to injury, not only were self-employed workers hit the hardest by Covid-19 lockdowns, but they also face barriers in accessing emergency interventions available to employed workers (Anderson, 2020).

The combined effect of employment insecurity and financial insecurity has affected not only labour market outsiders, but also labour market insiders, overcoming the division between outsiders and insiders in the social investment agenda. Crucially, it has contributed to the decline of the middle class or to the emergence of the so-called 'squeezed middle'. We now have solid evidence that the fortunes of the middle-class are shrinking in Europe, in particular due to the loss of aggregate household income by middle-income households between 1991 and 2010 in most European countries, as a result of declining wages, rents and pensions

available to this segment of the population (Kochhar, 2017; OECD, 2019). The fortunes of lower-income groups 1991-2010 have also declined in several countries, but, confirming Milanovic's (2016) global analysis of income evolution, the relative loss for middle-income groups in Europe has been greater (Kochhar, 2017). This has led authors to theorise about the disappearance, or the dramatic decline, of a middle-class in Europe, as an effect of the erosion of middle income and wealth returns, explained mostly through the evolution of wages (Vaughan-Whitehead, 2016). The declining middle class has been defined as the 'squeezed middle', a term used to describe the intermediate social position of 'ordinary' families with intermediate/upper-intermediate levels of education, and stable jobs, but which face an increasing challenge in maintaining their lifestyles (Parker, 2013). These middle-income groups have been particularly affected by the financialisation of the European economy after the 2008 crisis (Deutschmann, 2011), as indicated by the current measures of financial capability, namely managing day-to-day financial transactions via a bank account; saving to meet one-off expenses; managing a loss of earned income; investing in a pension; and avoiding and reducing debt (Kempson and Collard, 2012). As underlined recently by Demertzis et al (2020), European societies are also

The call for an integration between social investment and inequalities requires an exploration of how social investment policies can be potentially extended to the majority of the population, including both those at risk of poverty and the 'squeezed middle'.

An integration between the economic and social dimensions of the Semester is necessary to consider the net balance of the former on the latter.

particularly vulnerable to ‘financial fragility’, namely to the financial shocks that are likely to occur during a pandemic. The decline of the middle also has important political effects: as demonstrated by several publications (Antonucci et al, 2017; Kurer, 2020), a threat of economic decline (not just material hardship in itself) among the majority of the population is also driving support for populist and anti-establishment formations that tend to hold eurosceptic views.

The stagnant fortunes of low-income groups, and the declining position of middle-income groups, both call for policies that diverge from business-as-usual. The ‘integrated’ focus on the ‘low’ and ‘middle’ income groups we propose here reflects a reignited interest in the progressive effect of universalistic social policy provisions. This evolution overcomes the approach centred on targeting and means-testing in poverty and social exclusion policies, which have not succeeded in meeting the Europe2020 goals of reducing poverty. As pointed out by several scholars, the targeted approach has suffered two main trade-offs: first, the trade-off between investing in human capital and reducing inequality through cash transfers and mechanisms of compensation; second, the trade-off between targeting/conditionality and redistribution policies (Cantillon, 2011; Cantillon and Van Lancker, 2013). The call for an integration between social investment and inequalities (Pintelon et al, 2013) requires an exploration of how social investment policies can be potentially extended to the majority of the population, including both those at risk of poverty and the ‘squeezed middle’.

1.2 CONSIDERING THE LOOP EFFECT OF ECONOMIC AND SOCIAL POLICIES

The second element behind our definition of inequality concerns the divide between the economic and the social, and the neglect of their interdependence.

Crespy and Menz have noted that EU “social policy is becoming increasingly... subsumed to economic objectives focused on competitiveness, narrowly defined as low labour costs... and stringent fiscal discipline” (Crespy and Menz, 2015: 199–200). According to Copeland and Daly, the European Semester has contributed to subjugating other policies, including social policies, to macroeconomic criteria (budgetary discipline and correcting macroeconomic imbalances) (Copeland and Daly, 2018 150). The evidence of a socialisation of the European Semester (Jessoula, 2015; Zeitlin and Vanherke, 2018) focuses on the development of the social policy pillar and its increasing importance within the European Semester framework. An important element that is missing, however, is the mutual interaction between the two areas – ‘economic’ and ‘social’ – that have been developed as separate silos. What we are proposing is considering the ‘net socio-economic effect’ of the Semester recommendations.

To explore the relationship between the social and the economic, some authors have analysed the effect of social policy on market strategies. Copeland and Daly (2018), for example, have distinguished between social policies

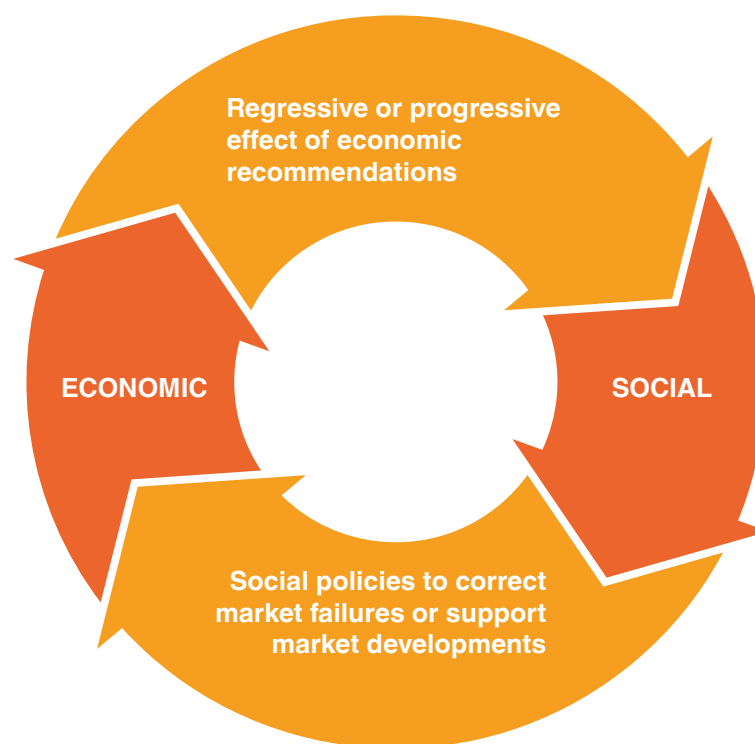


Figure 1. The interaction between economic and social policies

oriented to supporting market developments (pure ‘social investment’ policies) and social policies correcting market failures (using the old ‘redistributive’ framework). Another important dynamic to grasp is the effect of economic policies, distinguishing between those that are progressive in terms of social policy impact, and economic measures that are regressive (see the analysis of the effects of austerity packages in Europe by Theodoropolou and Watt, 2011). This second effect is potentially far greater in its influence than the (potential) effect of social policy on the economic sphere. Indeed, macroeconomic policies directly affect spending on services, which are crucial in reducing inequality. An integration between the economic and social is necessary to consider the net balance of the European Semester (a macroeconomic imbalance procedure) on the social sphere.

More specifically, this means evaluating the progressive or regressive effects of economic CSRs formulated through the European Semester for socio-economic inequalities. As suggested by Byrne and Ruane (2017), spending on services reduces inequality and therefore cuts in public spending on services have a regressive effect. This is particularly important to consider given the findings of the SOLIDAR Social Rights Monitor showing a regressive effect in the use of healthcare (for example in Greece), housing, care services and disability services in many European countries. Furthermore, access to education has a different effect on reducing social mobility across countries, with stark differences across EU countries (OECD, 2018). Our analysis is not therefore limited to measuring access to services per se (in line with current EU recommendations), but takes into account the regressive effect of declining public spending on services.

1.3 CONSIDERING WHO PAYS FOR STATE PROVISIONS AND WHO RECEIVES THE REWARDS

One of the most important findings of recent studies on inequality has been the effect on wealth (Piketty, 2014) and the re-configuration of the dynamic of income inequality (Milanovic, 2016). As stressed by Atkinson, part of the importance of the recent focus on wealth concerns the need to focus on the inequality of economic resources, going beyond the focus on inequality of opportunities emphasised in the previous social investment focus. Indeed “even if there were competitive equality of opportunity, the reward structure is too unequal and that ex post inequality needs to be reduced” (Atkinson, 2014). In order to look at the reward/paying structure, this dimension will consider both who contributes to public financing and who receives the rewards. Progressive taxation is a crucial element of this equation: the share of profits from inheritance during the post-second world war period was not achieved only through redistribution, but also through progressive taxation (Atkinson, 2014).

The analysis of taxation and inequality by Byrne and Ruane (2017) clarifies what ‘progressive taxation’ means in practice in current welfare states, by considering direct and indirect effects of taxation. Some key findings follow.

- ♦ The analysis confirms the need to re-organise the taxation base and the need to redistribute towards low- and middle-income groups in order to reduce overall inequality. The analysis, focussed on the UK, shows that most middle- and low-income households suffered a greater loss as a proportion of net household income than the richest 10 per cent of households. The changes that the authors describe go be-

yond the UK: the falling wage share has occurred across Europe and has been borne in the UK and elsewhere in Europe almost entirely by middle- and lower-paid employees (in the UK the bottom 60 per cent of earners, in Germany the bottom 55 per cent, in France the bottom 57 per cent and in Denmark the bottom 65 per cent). The other side of this coin is the fact that the share of income accruing to the top 1 per cent and 5 per cent has increased and has not been counter-balanced by an increase in taxation focussed on these groups.

- ♦ The analysis shows that countries in which total tax revenues are a relatively high proportion of GDP tend to be countries that have a relatively low degree of inequality (compare this to EU macroeconomic recommendations on competitiveness). A broad tax revenue is particularly important in supporting effective spending and increases access to services, which, as seen in the previous section, tends to reduce overall inequality.
- ♦ There has been a regressive shift in the tax burden, where a higher proportion of total tax revenues come from consumption rather than income and from labour (taxation on workers) rather than capital.
- ♦ There is a lack of progressivity in wealth taxation. Wealth and inter-generational transmission of inequality is not bad per se – the issue is on wealth concentration and on the redistributive effects of the recommendations on taxation. Wealth dispersion can also be used to improve the position of individuals with lower-middle incomes: “The redistribution of wealth is as much about the encouragement of small savings at the bottom as it is about the restriction of excesses at the top” (Atkinson, 2014).

2. WHY THE CURRENT EUROPEAN SEMESTER DOES NOT ADDRESS INEQUALITIES: AN ANALYSIS OF INDICATORS AND COUNTRY-SPECIFIC RECOMMENDATIONS

Drawing on the operational definition of inequality set out above, this second part of the policy paper proposes an in-depth analysis of the evolution of the Semester focusing on the latest cycle 2019. The aim is to trace how the issue of inequality is addressed in three main policy areas: overall social policies (labour market, education and social protection policies); public finance and economic policies; and taxation policies (including labour, corporate and capital income taxes, taxes on immovable property, net wealth and inheritance taxes, VAT and environmental taxes). To do so, we propose, firstly, an assessment of the indicators used in the Joint Employment Report (JER) and the Alert Mechanism Report (AMR) by DG EMPL, DG ECFIN and DG TAXUD at the European Commission, in the three policy areas identified above. Our assessment will be performed by looking at the relevance of the indicators for the item addressed, and their capacity to account for the inequality dimension of the phenomenon measured. Secondly, we perform an analysis of the country-specific recommendations addressed to member states in 2019, with the aim of understanding the distributional impact of the policy reforms addressed to member states based on the current set of indicators.

1. With regard to the proposal of addressing socio-economic insecurity beyond poverty, and by drawing and expanding on Corti (2020), we categorise each recommendation contained in the CSRs into four groups, according to the orientation of the policy prescription: social retrenchment, social investment, so-

cial inclusion and ‘tackling inequalities’ (namely specific recommendations that address inequalities as defined in the first part of this policy paper). The first group regards those recommendations that envisage the retreat of the State as the key provider of social solidarity in terms of both benefits and social rights, and that involve the adoption of ‘re-trenchment’ measures, such as social benefit curtailment, cost-containment strategies, labour-market deregulation or pension privatisation. The second group concerns the social-investment recommendations, which mainly aim to prepare, support and equip individuals to increase their chances of participating in the labour market. We then distinguish between recommendations oriented to the activation of the targeted population (social investment activation) and recommendations whose main objective is to provide individuals with skills and capabilities (social investment upskilling). The third group concerns social inclusion recommendations, which are intended to include socially excluded and targeted groups in various areas (education, access to healthcare etc). The fourth group identifies policies that have a positive redistributive impact, namely addressing emerging inequalities, redistributing resources towards middle- and lower-middle groups, and having a positive effect on the majority of the populations in the member states (thus beyond socially excluded groups).

2. With regard to the effect of economic policies on social policies, we draw on Theodoropolou and Watt (2011) and categorise all the CSRs on public finance and economic policies into two main groups: progressive and regressive prescriptions. This distinction is based on the overall income distributional effects of reforms of the public budgets on high, medium or low incomes. We define regressive recommendations as those calling for budgetary cuts to public services or government transfers, which would theoretically mostly benefit people from lower- to middle-income households (e.g. healthcare, pensions and education). Recommendations calling for a recalibration of welfare expenditure from traditional universal compensatory policy to new targeted social investments is not regressive per se, but can have a regressive effect if not accompanied by attention to the distributional effects on low- and middle-income classes, and of the potential expenditure shift from one policy to another. Conversely, we define progressive recommendations as those recommendations either calling for an increase in public expenditure on public services and government transfers that would mainly benefit low- and middle-income class or calling for an increase in public investments in sectors with high distributional income potential.
3. With regard to the side of who contributes to financing the taxation system and is directly or indirectly rewarded by it, drawing on Atkinson (2014) and Byrne and Ruane (2017), we look at the

inequality of economic resources, by focusing on the progressiveness of the taxation systems. Notably, we first divide CSRs on taxation into six groups, according to their content: i) recommendations on aggressive tax planning; ii) recommendations on labour taxation; iii) recommendations on second earners or low-income earners' taxation; iv) recommendations on wealth related taxes; v) recommendations on preferential tax treatment; and vi) recommendations on tax collection and tax compliance, fighting tax evasion. Based on the expected distributive effect, we qualify the orientation of the recommendations in three categories: regressive, progressive and neutral. Regressive taxation policies refer to measures which lack progressivity, i.e. they tend to collect payments or resources from many equally, with a consequent impact on low- to medium-income as well as on high-income groups, and with unavoidable consequences in terms of the fairness and equity of the taxation system. Conversely, progressive taxation policies redistribute resources in society from one group to another (Robin Hood effect) and have a positive impact in terms of inequality reduction (if the transfer is from higher- to medium- to lower-income households). Some examples are the recommendations on increasing wealth taxes, reconsidering preferential tax treatment, and fighting against aggressive tax planning. Neutral recommendations are those without an explicit direct effect on inequality, such as the recommendations on tax compliance.

2.1 GOING BEYOND POVERTY AND SOCIAL EXCLUSION IN THE SEMESTER: THE MISSING FOCUS ON SOCIAL AND EMPLOYMENT INEQUALITY

Within the European Semester, several social and employment indicators are used to monitor the performance of the member states. Overall, we can identify three sets of indicators used to monitor the social and employment performance of the EU27 member states: the Joint Employment Report (JER) scoreboard, which since 2017 has been based on the Pillar's social scoreboard, the Social Protection Performance Monitor (SPPM) scoreboard, and the Employment Performance Monitor (EPM) scoreboard. Table 1 in Annex II of this report presents the full list of social indicators used in the framework of the European Semester, divided into three main policy areas:

- ♦ education: childcare, primary to tertiary education, adult learning, vocational training;
- ♦ labour market: active labour market policies (ALMPs), social security system, wage bargain, unemployment benefit, labour protection, gender policies, youth initiatives, public employment service, subsidy schemes, access to finance for enterprises;
- ♦ social protection: social transfer and social assistance schemes, social service organisation and access, measures for combating poverty and social exclusion in different areas and in specific target populations, minimum income, access to healthcare.

What emerges in Table 1 is that the only indicator that explicitly measures economic inequality is the 'Quintile ratio S80/20', which is calculated as the ratio of the total income received by the 20 per cent of the population with the highest income (i.e. top quintile) to the income received by the 20 per cent of the population with the lowest (i.e. bottom quintile).² While this indicator has the advantage of being easy to understand, it potentially omits important households in the income hierarchy. Indeed, since it is based on the outer 20 per cent at both ends of the income distribution, it does not consider the whole distribution of income. In this respect, Palma (2018) shows that the distribution of inequality in Europe largely concentrates in the bottom 40 per cent plus the top 10 per cent. Accordingly, measures of inequality that are comprehensive and that incorporate the middle groups are not always optimal given the prominence of the top and bottom groups in driving distributional change. Palma therefore suggests focussing on the ratio of the income of the top 10 percent to the bottom 40 per cent, or even just the share of the top 10 per cent alone (Palma, 2018).

Inequality is not only measured by looking at the Quintile ratio S80/20. Other important indicators are the rate of people at risk of poverty (AROP), the rate of people living in a household with a very low work intensity, and the rate of people in severe material deprivation. The first indicator refers to individuals, whose equivalised disposable income is less than 60 per cent of the median. The second refers to people, who work less than 20 per cent of their potential working time. The third indicator re-

The only indicator that explicitly measures economic inequality is the 'Quintile ratio S80/20'.

² The unit of analysis is typically equivalised household income per person, not individual income. Equivalised means household income per person is adjusted slightly to account for household composition, so two people living together and sharing costs with a combined income of €50,000 are deemed to have a higher income than the same two people living separately with incomes of €25,000 each. Children are also deemed to consume less than adults so that a two-adult household with €50,000 has a lower equivalised income than the same amount spread between an adult and child.

While it has the advantage of being easy to understand, it potentially omits important households in the income hierarchy.

fers to those unable to afford some items considered by most people to be desirable or even necessary to lead an adequate life. These indicators are of absolute importance for measuring inequality of outcomes, and they focus especially on the bottom of the income distribution. They thus look at the most vulnerable in society, namely those living in conditions of poverty and social exclusion. The same holds true for all the other indicators that are listed in Table 1 in the area ‘social protection’ and refer to people at risk of poverty, measured in terms of equivalised disposable income, and to people in severe material deprivation. Despite some concerns in terms of time lag and volatility (Istituto per la Ricerca Sociale, 2016), the indicators used in the framework of the Semester to measure poverty and social exclusion are widely considered robust and comparable.

As we have stressed earlier, however, socio-economic inequalities are not only linked to poverty and social exclusion, but also to employment and financial insecurity or inequality in access to services.

With respect to employment security, the current scoreboard of indicators used for the Joint Employment Report only partially focuses on inequality. The focus mainly rests on unemployment and the employment rate. Indica-

tors that concern employment insecurity (for instance, the incidence of atypical/non-standard jobs on employment, including part-time work, temporary work, fixed-term work, casual and seasonal work, self-employed people, independent workers and homeworkers) are missing. Indicators on the distribution of these forms of employment among low- or high-skilled workers, and more general indicators on the occupational class of these workers should be provided in order to measure employment inequalities. More recently, new indicators have been added, which measure, for instance, the rate of people in-work at risk of poverty, the rate of involuntary part-time and temporary employment, and the rate of inactivity and part-time work due to personal and family responsibility. However, these indicators cannot be considered as enough to take into account inequalities linked to employment insecurity. The Covid-19 crisis has unveiled how digital literacy and access to computer devices or the internet have a significant impact on inequalities. Just recently, the Social Scoreboard has introduced a new indicator on the level of digital skills among individuals aged 16-74. However, no indicators are included as concerns the digital divide that mostly affects the medium- to low-income workers.³

To prove the point that the current set of indicators lacks a comprehensive focus on inequali-

Indicators that measure employment insecurity, such as the incidence of atypical/non-standard jobs on employment, including part-time work, temporary work, fixed-term work, casual and seasonal work, self-employed people, independent workers and homeworkers, are missing in the Semester.

³ An example is indicators on the population with no access to broadband 100/20, with no internet access and no computer devices. These indicators, which are provided by the Digital Divide Index, should be integrated.

ty, we analysed the CSRs that were addressed to all EU member states in 2019 in the field of social and employment policies, in particular dividing recommendations into four policy areas: labour market, social protection, health, and education. What emerges is that, firstly, 69% of the recommendations addressed to member states in the sphere of labour market policies present a specific focus on activation and employability, and 7% on inclusion of disadvantaged groups in the labour market, but they lack attention to inequalities. Only 21% of the labour market recommendations explicitly address tackling inequalities, and mainly refer to the need to reduce the fragmentation of the labour market, to promote and extend adequate social protection for non-standard workers, and higher minimum wages. Attention is paid to the integration of disadvantaged groups in the labour market, as well as to providing personalised active integration support and facilitating upskilling, supporting women's participation in the labour market, and increasing the employment rate of older workers, by strengthening life-long learning. A specific focus is therefore missing on the areas of labour market insecurity that affect the majority of workers described in the first part of this policy paper – areas such as the decline in job quality, job tenure insecurity and, above all, job status insecurity.

The area of social protection contains a high percentage of recommendations addressing social inclusion (73%) and only a minor percentage tackling inequalities (23%). Recommendations have a specific focus on countering poverty and social exclusion by guaranteeing adequacy of unemployment benefit, healthcare and minimum income. For example, Romania received a recommendation on increasing the coverage and

quality of social services and on completing the minimum inclusion income framework, as did Spain. Specific attention is also paid to the integration of minorities, notably Roma, for instance in Hungary and Slovakia. Overall, however, the approach to inequality in the field of social protection largely adopts a rather narrow definition of inequalities, which focuses on the bottom distribution of income and mainly on marginalised groups.

In addition to this, there is the problem of inequality in access to services. The current JER scoreboard does not indeed provide a full account of what we have called inequality of opportunities. An example is child poverty. Addressing inequality of opportunities for children implies looking at different aspects that primarily include precariousness of the family situation: child material deprivation and household disposable income, household composition (e.g. children living in single-adult household), social risks factors (e.g. children in Roma family). Children in a precarious family situation face several inequalities that can be measured in terms of inequality in access to key social services, such as adequate housing (e.g. severe housing deprivation, living in an overcrowded household, house cost overburden), healthcare (e.g. unmet medical needs), early childhood education and care (e.g. level of enrolment in formal childcare and pre-primary school), and free education (e.g. student performance by economic background). At the moment, only two indicators in the Semester look at children: 'children aged less than 3 years old in formal childcare' and 'children at risk of poverty or social exclusion'. These two indicators, however, are not enough to address the issue of child inequality. As for the former, the lack of disaggregated data on access to childcare on

the socio-economic background of pupils attending early childcare does not allow us to measure inequality in access among children from different households. However, measuring children's poverty by looking at the indicator on the AROP rate is problematic as we only consider people falling below 60 per cent of median income, thus excluding a large part of the middle class. By contrast, a good example of monitoring inequality in access to services is given in the area of education and training, where accessibility to education is linked to the socio-economic background of beneficiaries, and where recommendations prescribe member states to deliver education reform aimed at extending the coverage of education services.

All in all, we identify four main reasons why the Semester recommendations in the field of social and employment policies lack a proper inequality approach. First, the indicator chosen to actually measure inequality presents

significant shortcomings and does not take into account income distribution in a large and significant part of the population. Second, the other indicators used to measure income redistribution mainly focus on the distribution of income inequalities in the bottom part of the population. While this is certainly of great importance, it does not give us a complete overview of inequalities in a given society. Third, a large part of the inequalities related to job insecurity, financial insecurity and employment contracts is not measured since indicators are missing. Fourth, while social investment plays a key and central role in the Semester monitoring process, a focus on the inequality of opportunities is missing in some policy areas, such as childcare, where data on participation in early childcare are not disaggregated by household income of the beneficiaries, affordability (e.g. out of pocket expenditure) or the accessibility (e.g. geographical, infrastructural) of public services.

While social investment plays a key and central role in the European Semester, a focus on the inequality of opportunities is still missing in some policy areas, such as childcare.

2.2 THE EFFECTS OF MACROECONOMIC RECOMMENDATIONS ON INEQUALITY

As we stated in the first part of this policy paper, macroeconomic recommendations have a loop effect on inequality. In this section, we discuss the progressive or regressive effect of the existing recommendations on inequality.

Macroeconomic performances of member states are monitored in the European Semester in the so-called Alert Mechanism Report (AMR). Contrary to the Joint Employment Report, the AMR is embedded in a surveillance mechanism, i.e. the Macroeconomic Imbalance Procedure (MIP), the aim of which is to identify the “unsustainable trends” in the macroeconomic performance of each member state, to prevent and, if necessary, to correct the potential negative economic and financial spillover effects (negative externalities) which aggravate vulnerability. Table 2 in Annex II presents the set of headline indicators currently used in the AMR scoreboard and that function as an early warning mechanism. This determines whether there are imbalances that might unfold unsustainable trends and, in case of excessive imbalances, it activates either an Excessive Imbalance Procedure (EIP) or an Excessive Deficit Procedure (EDP).

All in all, the governance of the MIP, based on a strict prevention and sanctioning mechanism, and the choice of the indicators unveil a clear imbalance in the Semester’s approach

to public finance and economic policies, which instead mainly focuses on competitiveness and budgetary stability, de facto ignoring possible distributional effects of macroeconomic recommendations. In particular, the specific focus on budgetary expenditure and the strict monitoring on debt sustainability represents a very unfavourable territory for public investments. The explicit priority given to budgetary stability, embedded in a monitoring and sanctioning mechanism, defines the boundaries for the action of member states and significantly hampers their fiscal capacity. The attention paid mainly to the level of expenditure and not to the kind of expenditure de facto risks having a regressive impact on the levels of public expenditure on public services. This unfavourable environment has unavoidable consequences in terms of member states’ capacity to address inequalities, whereas the constraints posed for countries experiencing imbalances in levels of debt to GDP also directly affect key expenditure sectors such as healthcare and education, which theoretically would mostly benefit people from lower- to middle-income households.

A look at the macroeconomic recommendations in the cycle of the 2019 Semester immediately unveils a persisting focus on budgetary stability and debt reduction (which has a regressive effect on overall inequality), as well as a limited focus on public investment. All the macroeconomic recommendations addressed to member states have an explicit regressive effect. For instance, Italy is requested not only to reduce its net primary government

The attention paid mainly to the level of expenditure and not to the kind of expenditure within the Macroeconomic Imbalance Procedure risks having a regressive impact on the levels of public expenditure on public services.

expenditure but also to use windfall gains not to relaunch public investment but to accelerate the reduction of its general debt ratio. The same recommendation is addressed to Portugal, Belgium, France, Ireland and Spain. Particular attention is paid to the sustainability of the pension system and the reduction of expenditure in this sector, which indeed remains constantly under strict monitoring. Additionally, particular attention is also paid to the sustainability of the healthcare sector. Sixteen member states in fact are recommended to ensure the fiscal sustainability of their long-term care and pension systems, for instance by limiting early exit possibilities from the labour market and adjusting the statutory retirement age in view of expected gains in life expectancy. All in all, although the macroeconomic framework defined in the Semester does not directly hamper government expenditure by asking for cuts and reductions, as was the case in the early Semester cycles, it indirectly affects member states' capacity to use public resources to redistribute and conduct public investments, by setting tight constraints and setting the limits of governments' initiative.

In the case of the pensions sector and healthcare, explicit recommendations are made on the need to increase cost-effectiveness and sustainability in the long term. In this scenario, there is no focus on the potential consequences of the recommendations made to member states on inequalities. The goal of making the pension system sustainable in order to guarantee intergenerational fairness should not be to the detriment of addressing intra-generational inequality and, in particular, the widespread inequality in pension levels between high pensions and low-middle levels of pension. Without addressing these existing inequalities, the recommendations on pensions have a regressive effect on the overall income distribution. For example, the recommendation addressed to Italy in 2019 states: "Implement fully past

pension reforms to reduce the share of old-age pensions in public spending and create space for other social and growth-enhancing spending". The Commission rightly points out that Italian expenditure on old-age pensions, at around 16% of GDP (above one third of total government spending!), is among the highest in the Union and – especially after the re-introduction of an early retirement scheme – this risks worsening the sustainability of public finances in the medium term. Similarly, the Commission is right in explaining that high public spending for old-age pensions restrains other social and growth-enhancing spending items like education and investment. However, attention should also be paid to reducing the share of public expenditure for pensions. While the proposal of the Commission is to be welcomed as regards intervening on the high pension entitlements not matched by contributions, explicit reference should be made to ensuring adequate low- to middle-pensions in order to guarantee an even distribution of benefits. Even clearer is the case of Ireland, which received a recommendation asking it to "address the expected increase in age-related expenditure by fully implementing pension reform plans". In this case, the focus on the redistribution of pension benefits to medium to low income is completely absent and there is no specification – as in the case of Italy – on how to put the pension system on a more sustainable footing (e.g. by intervening on high-pension income). By contrast, a positive example of a recommendation on sustainability of the pension system, which at the same time addresses the issue of inequality, is that made to Slovenia. In this case, the Commission asks the Slovenian government to adjust the statutory pension age in line with increased life expectancy and to promote early retirement. At the same time, however, it stresses the need to ensure adequate pensions, as almost 40 per cent of single people aged over 65-years old in Slovenia are at risk of poverty.

2.3 THE RECOMMENDATIONS ON TAXATION AND THEIR EFFECTS ON INEQUALITY: A MISSED OPPORTUNITY?

As we have seen in the first part of this policy paper, taxation is a central mechanism for addressing growing socio-economic inequalities. Taxation is also one of the key areas monitored in the European Semester. While monitoring taxation policy varies significantly from country to country (and the Commission itself acknowledges that the results of monitoring always need to be interpreted alongside in-depth country analysis before any conclusions can be drawn as to appropriate policies), we can still identify some main patterns in the Commission's approach to taxation. In this respect, taxation sections in country reports focus on the following issues: the ratio between taxation revenues and GDP; taxation structure according to economic functions (labour, capital, corporate, consumption); breakdown analysis of composition of labour taxation; corporate taxation, which includes corporate income taxation and other taxes on production; capital taxation, including property and wealth; value added tax, including reduced rates; tax compliance; and environmental taxation. In analysing taxation policies, the overall attention of the Commission is placed on the efficiency of the taxation system, and its capacity to boost economic growth and to effectively support budgetary expenditure. However, the issue of inequality and the redistributive impact of taxation policies is mainly left aside and emerges in an unsystematic way in some member states' country reports but not in others. Still, the Commission itself in its biannual report on 'Tax policies in the Eu-

ropean Union', which represents the basis of the Semester's analysis, explicitly recognises the key role of taxation in reducing inequalities and supporting social mobility, be it through pre-distribution, redistribution, or correcting or incentivising behaviours. In particular, three taxation policies are indicated by the Commission as especially efficient in tackling inequalities: (i) wealth transmission, individuals' capital income and property taxation, which contributes to increasing the progressivity of the overall tax mix, thus mitigating wealth inequality and supporting equality of opportunity; (ii) progressive personal income taxation, which contributes to reducing disposable income inequality; (iii) targeted population taxation, especially low-income taxation, designed in order to create jobs, thus reducing social exclusion and poverty.

The analyses provided in the country reports shows that the issue of inequality in the Semester is addressed firstly by looking at the progressivity of personal income taxation, which is measured by comparing the tax wedges on high- and low-income earners (represented respectively by individuals with an income above 167 per cent or up to 50 per cent of the average income). Attention to the difference in tax burden for different personal income tax levels has a specific focus on low-income taxation, whereas lower taxation is considered a positive incentive to include people outside the workforce in the labour market (especially low-skilled workers, young people, the elderly and second earners), and at the same time to reduce poverty and social exclusion. By contrast, there is no specific attention paid to specific schemes for top earners, which usually target expats on a gross income above a certain threshold, or certain professions (the existence of these schemes

The attention to the progressivity of personal income taxation is primarily oriented to the efficiency and productivity of the labour market rather than redistributing resources especially towards middle and lower-middle groups.

No recommendations are addressed to wealth related taxes to make the system fairer, including via inheritance or gift taxes, nor to preferential tax treatment, such as for high-income schemes.

usually create competition between member states and deprive countries of the taxes that are due). This confirms that the attention to the progressivity of personal income taxation is primarily oriented to the efficiency and productivity of the labour market rather than redistributing resources especially towards middle and lower-middle groups.

Tax credits and the degree of joint taxation can also contribute to high marginal tax rates for second earners moving from inactivity into work. In order to measure income inequality, one should look at the power of the tax and benefit system to correct income inequality. This is done by looking at: (i) the difference between market income inequality (including pensions from market income) and disposable income inequality (before social transfers), which shows the redistributive impact of taxes on income inequality; and (ii) the difference between disposable income inequality before and after social transfers, which shows the extent to which social transfers reduce it.

As concerns wealth taxation, the Semester's focus is on property taxation, and especially recurrent taxation, which is considered as a more growth-friendly source of revenue compared to taxes on labour. In terms of addressing inequality, the support expressed in the Semester for property taxation takes into account the distributional impact and applies accordingly ad hoc exemptions to low-value properties and low-income pensioners, while focusing especially on luxurious properties. Another important area which is monitored in the Semester is the progressivity of taxation on inheritance/gift and capital gains, which can help reduce wealth inequality and support social mobility by reducing the extent to which wealth inequalities are transmitted from one

generation to another. While labour income taxation, property taxation, capital income taxation, net wealth taxation and inheritance taxation have a clear distributive effect and can therefore be directly associated with the capacity to tackle inequalities, it is worth underlining that other kinds of taxation can have a significant distributive effect and therefore have an impact on inequalities. For instance, corporate income taxation contributes to a shift of the tax burden to less mobile tax bases (e.g. labour), with consequences in terms of inequality and burden-sharing. Value added taxation (VAT) has a direct impact on all consumers and its impact is usually regressive. Reduced rates are not effective in terms of redistribution as they cannot target a specific group (e.g. low-income population).

Moving to the content of taxation recommendations addressed to member states in 2019, we first observe that four are addressed to shifting the tax burden away from labour; four are addressed to a tax system that facilitates aggressive tax planning; three are addressed to improving tax collection and tax compliance, and to fighting tax evasion; and one is addressed to reducing the tax wedge for low-wage and second earners. No recommendations, however, are addressed to wealth related taxes to make the system fairer (including via inheritance or gift taxes) nor to preferential tax treatment (e.g. for high-income schemes). As concerns the orientation of the recommendations, the CSRs hardly make any reference to a progressivity of taxation system.

Most recommendations propose a reconfiguration of the taxation mix (without specifying the progressivity of the taxation). The main issue with these proposals is the lack of specific reference to the balance in the taxation

mix. In the case of Germany, for instance, the recommendation is to lower the tax wedge for low-income earners, increase the progressivity of social security contributions, and increase environmental taxes, while at the same time alleviating the impact of the latter on the vulnerable population. In Italy, the same recommendation suggests increasing taxation on first residences for high-income households and on consumption, by reducing reduced rates. Neither in the case of Germany nor in the case of Italy is there a clear recommendation on how to reduce taxation on labour, or on the balance between employers' and employees' contributions and on the distributional effects of those reforms.

In a few countries, we find recommendations to increase the tax base, which is potentially a progressive taxation measure, given the focus on increasing taxation on capital. These recommendations suggest addressing features of the tax system that may facilitate aggressive tax planning by individuals and multinationals, in particular by means of outbound payments.

This group of recommendations is addressed to countries that have particularly capital-friendly taxation, namely Malta, Cyprus, Ireland, the Netherlands and Luxembourg – the taxation systems of which, by creating unfair competition with other member states, de facto deprive the other countries of the taxes that are due, and thus of resources that could be used to tackle inequalities. Finally, in a minority of Baltic states with particularly regressive taxation systems (Latvia and Lithuania) the recommendations make explicit reference to progressive taxation reforms. We have highlighted these recommendations in the table in Annex I. They could be used as a basis for progressive taxation recommendations.

Overall, the analysis of the CSRs addressed to member states in 2019 does not show any explicit strategy to tackle inequality. Indeed, the areas targeted in the country reports, such as inheritance taxation, are not translated into country-specific recommendations, which suggests that a more comprehensive approach to inequality is needed.

3. RECOMMENDATIONS: HOW TO ADDRESS INEQUALITIES VIA THE EUROPEAN SEMESTER

The aim of this section is briefly to recall the main findings of the previous analyses and provide recommendations in order to improve the Semester's capacity to tackle inequality. In doing this, we will also explicitly discuss Covid-19 as a window of opportunity for the implementation of reforms and for rethinking the distributional effect of those measures.

RECOMMENDATIONS PART 1: SOCIAL POLICY BEYOND POVERTY AND SOCIAL EXCLUSION

As highlighted above, the combined effect of employment insecurity and financial insecurity has affected not only labour market outsiders, but also labour market insiders. Our analysis overcomes the division between outsiders and insiders, as it considers how emerging labour market risks and the growing financial insecurity affect 'the squeezed middle'. So far, the European Semester is devoid of indicators that measure the inequalities in terms of working conditions within the labour market and financial insecurity. To this end, the objective of this section is to provide a new set of indicators to measure the level of such inequalities, by using the existing principles of the EPSR (secure and adaptable employment, wages, information about employment conditions and protection in case of dismissals, social dialogue and involvement of workers and work-life balance) and by going beyond them to capture emerging forms of insecurity and socio-economic inequality.

In Section 2.1 we discussed the limits of the indicators currently used both in the Joint Employment Report and in the Alert Mechanism Report in grasping socio-economic in-

equalities linked to labour market insecurity and job quality (in particular, job-tenure and job-status insecurity), financial insecurity and the distribution of income and wealth. We have therefore elaborated three sets of recommendations that are related to the use of new indicators (see Annex III for the full list).

1. Include indicators of work that capture the declining quality of work among the majority of workers (namely indicators of job-status insecurity, job quality and work representation). As discussed in the first part of this policy paper, the current European Semester cycle lacks an understanding of the declining features of work in Europe that concern not only labour market outsiders (those in 'lousy jobs'), but also so-called labour market insiders. We have therefore added in Annex III (B) a number of indicators that deal with: employment insecurity and job status insecurity (indicator B.a); social dialogue (B.b); working time and work-life balance (B.c); and overall job quality (autonomy, work intensity and work relationships) (B.d) from the European Union Labour Force Survey (EU-LFS) and Eurofound. Following up on the proposal by Leschke and Watt (2014), we also promote the set-up of an EU Job Quality Index (JQI) multi-dimensional indicator that can be included in EU official datasets and used to monitor how national reforms are influencing the quality of work in the European Semester.

2. Include indicators of financial capability and financial fragility to monitor financial insecurity in the European Semester.

Recent studies have demonstrated that in the majority of EU countries, most households have savings equivalent to just a few weeks of basic consumption. One in three EU households is unable to meet an unexpected shock during regular times, a risk that increases during the pandemic (Demertzis et al, 2020). We propose, therefore, including indicators of financial insecurity that measure the impossibility of repaying unexpected expenses, and the impossibility of repaying accumulated debt, and measures of financial capabilities (Kempson and Collard, 2012), namely: managing day-to-day financial transactions via a bank account; saving to meet one-off expenses; managing a loss of earned income; investing in a pension; and avoiding and reducing debt. Some of these indicators are already available in EU official data – for example, indicators on household inability to meet an unexpected required expense, disaggregated by all households (Annex III, indicator C.a), households with or without dependent children (C.b), and single person households with dependent children (C.c) are available from the EU Statistics on Income and Living Conditions (EU-SILC) survey and should therefore be included in the European Semester monitoring. Other indicators of ‘financial fragility’, defined as the capacity to respond to financial shocks, which could be included in the Semester are the median household savings in relation to either income or needs for basic spending (C.d) and the median monthly gross income per household (C.e), both from the European Central Bank (ECB) Household Finance and Consumption Survey.

3. Use measures of income and wealth inequality within countries pre and post taxes in the European Semester

(Annex III, indicator A) in order to account for the redistributive effects of the policies included in the CSRs. We also note that a more comprehensive approach to equality in opportunities for access to services, in addition to the approach already established in education policies, should be developed. This area would look, for instance, at disaggregated data (per household income decile) on access to early childcare, out-of-pocket expenditure for childcare services, the number of free hours guaranteed per child per week etc. (Annex III, indicators D).

RECOMMENDATIONS PART 2: CONSIDER THE EFFECT OF MACROECONOMIC POLICIES ON SOCIAL POLICIES

As illustrated earlier, three main problems have emerged from the analysis of the relationship between the macroeconomic policies of the Semester and their effect on socio-economic inequalities. The first problem regards the set of indicators currently used in the macroeconomic imbalance procedure and especially the limited number of social indicators and their incapacity to account for inequalities. The second problem refers to the governance of the Semester and the quasi-automatic sanctioning mechanism of the Excessive Deficit Procedure and the Excessive Imbalance Procedure, which are activated in the case of a member state reaching the established threshold, without any consideration upon the possible negative externalities on social expenditure and public investment. Finally, the third problem, which is still related to the governance of the MIP, regards the involvement of a very restricted groups of actors, mainly limited to DG ECFIN in the Commission and the finance ministers and the Economic and Financial Committee (EFC) and the Economic Policy Committee (EPC) in the Council.

Against this background, we propose the following three recommendations in order better to consider the effect of macroeconomic policy on social expenditure and therefore social inequalities:

4. Integrate the current set of headline indicators in the MIP with the auxiliary indicators to better take into account household financial fragility. In particular, we propose integrating the current indicator on private sector debt with additional indicators on the assets, liabilities, income and consumption of households, which are available from the ECB Household Finance and Consumption Survey (HFCS) (Demertzis et al, 2020) (see Annex III, indicators C). We then propose accompanying the indicator on nominal unit labour cost (NULC) with auxiliary indicators on the levels of compensation of employees per hour worked (e.g. adjusted nominal increases by the consumer price index for each country).

5. Revise the EU fiscal framework and especially the expenditure rules of the Stability and Growth Pact in the framework of the debate on the review of EU economic governance (European Commission 2020a) and in light of the decision to activate the general escape clause (European Commission 2020b). Our analysis has indeed shown the regressive effects of macroeconomic recommendations on member states' capacity to use public resources to redistribute and conduct public investments, by setting tight constraints on budgetary expenditures and especially doing so without paying due consideration to the possible negative externalities on the most vulnerable categories. In line with Gros and Jahn (2020), we therefore recommend first the adoption of a golden rule in the Stability and Growth Pact, which would exempt net investment spending from the relevant deficit targets of both the preventive and the corrective arm of the SGP, in order to provide an incentive for a government to undertake at least the maintenance expenditure needed to keep the capital stock intact.

Secondly, we recommend rephrasing the SGP-based recommendations to member states in a way that takes into account the distributional effects and notably the possible regressive effect of budgetary consolidation recommendations on potential beneficiaries of public spending for social services (a good example is the recommendation on the adequacy of its pension system addressed to Slovenia in 2019).

6. Involve the social actors in a formalised way in the drafting process of the macroeconomic recommendations. At the moment, the drafting process of macroeconomic recommendations remains firmly in the hands of DG ECFIN in the Commission and of the EFC/EPC configuration in the Council. Although the economic actors have a say on social and employment recommendations (DG ECFIN has the last word on the country report), this is not the case for the social actors. In a similar vein, while social partners are now regularly consulted by DG EMPL in the context of the Semester process, this does not hold true for DG ECFIN which, however, decides on recommendations related, for instance, to wages.

RECOMMENDATIONS PART 3: PRIORITISE TAXATION

Our analysis of taxation has shown that the European Commission already engages in a biannual monitoring of taxation policies across countries, which is then used as background analysis for the Semester's country report. Such analysis already takes due account of the impact of regressive taxation systems on inequalities. Most notably, as observed above, specific attention is paid to the progressivity of taxation system, increasing wealth related taxes, tackling aggressive tax planning, and reviewing the preferential tax system. Nevertheless, when it comes to recommendations to member states, there is a gap between the analyses and the recommendations. Indeed, the CSRs focus mostly on the efficiency of taxation systems, competitiveness, and productivity. In order to use the Semester better to take into account the paying/reward structure of the taxation systems and assess its progressiveness, we have three main recommendations:

7. Expand and use consistently the progressive taxation recommendations that are currently made for countries with competitive taxation arrangements. The 2019 round of European Semester recommendations contains a small number of progressive taxation recommendations for a few countries that can be used as 'best practice' for the formulation of recommendations (see the Annex I recommendations in orange for the 2019 cycle). An example of this is the recommendation for Latvia – "Reduce taxation for low-income earners by shifting it to other sources, particularly capital and property, and by improving tax compliance" – that can be an example of a progressive recommendation on taxation.

8. **Have a coordinated approach to EU tax erosion.** Another reason why it is crucial to have consistent recommendations on taxation is to avoid 'taxation dumping' by countries with particularly generous tax incentive regimes. In this sense, taxation recommendations can serve to address horizontal inequalities between member states, not only to tackle vertical inequalities, in order to avoid fragmentation in taxation regimes and the race to the bottom of the taxation systems through the backdoor.

9. **Expand the tax base in a progressive way.** More recently, new tax instruments have been introduced by member states in new areas not just to increase the tax base, but also to serve as disincentives to individuals' choices and behaviour (e.g. in the areas of urbanisation, climate change, energy consumption). The calls to expand the tax base can have a potentially positive effect on net inequality *if* they take into account the distributional effects of those measures and are incorporated in conjunction with existing social policies.

ANNEX I

An evaluation of country-specific recommendations (2019) in relation to ‘inequality’

| COUNTRY (TOTAL CSRS) | COUNTRY-SPECIFIC RECOMMENDATIONS | ORIENTATION | AREA |
|--------------------------------|-------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|--------------------------------|-------------------|
| Austria Total no. 4 | Ensure the sustainability of the health, long-term care, and pension systems, including by adjusting the statutory retirement age in view of expected gains in life expectancy. | Regressive | Macro-economic |
| | Shift taxes away from labour to sources more supportive for inclusive and sustainable growth. | Reconfiguration taxation mix | Taxation |
| | Support full-time employment among women, including by improving childcare services, and boost labour market outcomes for the low skilled, in cooperation with the social partners. | Social investment – activation | Labour market |
| | Raise the levels of basic skills for disadvantaged groups, including people with a migrant background. | Social inclusion | Education |
| Belgium Total no. 4 | Ensure that the nominal growth rate of net primary government expenditure does not exceed 1.6% in 2020, corresponding to an annual structural adjustment of 0.6% of GDP. Use windfall gains to accelerate the reduction of the general government debt ratio. | Regressive | Macro-economic |
| | Continue reforms to ensure the fiscal sustainability of the long-term care and pension systems, including by limiting early exit possibilities from the labour market. Improve the composition and efficiency of public spending, notably through spending reviews, and the coordination of fiscal policies by all levels of government to create room for public investment. | Regressive | Macro-economic |
| | Remove disincentives to work and strengthen the effectiveness of active labour market policies, in particular for the low skilled, older workers and people with a migrant background. | Social investment – activation | Labour market |
| | Improve the performance and inclusiveness of the education and training systems and address skills mismatches. | Social investment – upskilling | Education |
| Bulgaria Total no. 4 | Strengthen employability by reinforcing skills, including digital skills. | Social investment – activation | Labour market |
| | Improve the quality, labour market relevance, and inclusiveness of education and training, in particular for Roma and other disadvantaged groups. | Social inclusion | Education |
| | Address social inclusion through improved access to integrated employment and social services and more effective minimum income support. | Social inclusion | Social protection |
| | Improve access to health services, including by reducing out-of-pocket payments and addressing shortages of health professionals. | Tackling inequality | Social protection |

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| Croatia Total no. 4 | Deliver on the education reform and improve both access to education and training at all levels and their quality and labour market relevance. | Social investment – upskilling/ activation | Education |
| | Consolidate social benefits and improve their capacity to reduce poverty. | Social inclusion | Social protection |
| | Strengthen labour market measures and institutions and their coordination with social services. | Social investment – activation | Labour market |
| | Reinforce the budgetary framework and monitoring of contingent liabilities at central and local level. Reduce the territorial fragmentation of the public administration and streamline the functional distribution of competencies. | Regressive | Macro-economic |
| Cyprus Total no. 4 | Complete reforms aimed at increasing the effectiveness of the public employment services and reinforce outreach and activation support for young people. | Social investment – activation | Labour market |
| | Deliver on the reform of the education and training system, including teacher evaluation, and increase employers' engagement and learners' participation in vocational education and training, and affordable childhood education and care. | Social investment – upskilling | Education |
| | Take measures to ensure that the National Health System becomes operational in 2020, as planned, while preserving its long-term sustainability. | Tackling inequality | Social protection |
| | Address features of the tax system that may facilitate aggressive tax planning by individuals and multinationals, in particular by means of outbound payments. | Increasing tax base | Taxation |
| Czech Republic Total no. 3 | Improve long-term fiscal sustainability of the pension and healthcare systems. Adopt pending anti-corruption measures. | Regressive | Macro-economic |
| | Foster the employment of women with young children, including by improving access to affordable childcare, and of disadvantaged groups. | Social investment – activation | Labour market |
| | Increase the quality and inclusiveness of the education and training systems, including by fostering technical and digital skills and promoting the teaching profession. | Social investment – upskilling | Education |
| Denmark Total no. 1 | Focus investment-related economic policy on education and skills, research and innovation to broaden the innovation base to include more companies, and on sustainable transport to tackle road congestion. | Social investment – upskilling | Education |
| Estonia Total no. 4 | Address skills shortages and foster innovation by improving the capacity and labour market relevance of the education and training system. | Social investment – activation | Labour market |
| | Improve the adequacy of the social safety net and access to affordable and integrated social services. | Social inclusion | Social protection |
| | Take measures to reduce the gender pay gap, including by improving wage transparency. | Tackling inequality | Labour Market |
| | Ensure that the nominal growth rate of net primary government expenditure does not exceed 4.1% in 2020, corresponding to an annual structural adjustment of 0.6% of GDP. Ensure effective supervision and the enforcement of the anti-money laundering framework. | Regressive | Macro-economic |

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| Finland Total no. 3 | Ensure that the nominal growth rate of net primary government expenditure does not exceed 1.9% in 2020, corresponding to an annual structural adjustment of 0.5% of GDP. | Regressive | Macro-economic |
| | Improve the cost-effectiveness of and equal access to social and healthcare services. | Regressive | Macro-economic |
| | | Access | Social protection |
| | Improve incentives to accept work and enhance skills and active inclusion, notably through well-integrated services for the unemployed and the inactive. | Social investment – activation | Labour Market |
| France Total no. 4 | Ensure that the nominal growth rate of net primary expenditure does not exceed 1.2% in 2020, corresponding to an annual structural adjustment of 0.6% of GDP. Use windfall gains to accelerate the reduction of the general government debt ratio. Achieve expenditure savings and efficiency gains across all sub-sectors of the government, including by fully specifying and monitoring the implementation of the concrete measures needed in the context of Public Action 2022. | Regressive | Macro-economic |
| | Reform the pension system to progressively unify the rules of the different pension regimes, with a view to enhancing their fairness and sustainability. | Regressive | Macro-economic |
| | Foster labour market integration for all job seekers, ensure equal opportunities with a particular focus on vulnerable groups including people with a migrant background and address skills shortages and mismatches. | Tackling inequality and social inclusion | Labour Market |
| | Continue to simplify the tax system, in particular by limiting the use of tax expenditures, further removing inefficient taxes and reducing taxes on production. Reduce regulatory restrictions, notably in the services sector, and fully implement the measures to foster the growth of firms. | Regressive | Taxation |
| Germany Total no. 6 | Focus investment-related economic policy on education. | Social investment – upskilling | Education |
| | Shift taxes away from labour to sources more supportive for inclusive and sustainable growth. Strengthen competition in business services and regulated professions. | Reconfiguration taxation mix | Taxation |
| | Reduce disincentives to work more hours, including the high tax wedge, in particular for low-wage and second earners. | Reconfiguration taxation mix | Taxation |
| | Take measures to safeguard the long-term sustainability of the pension system, while preserving adequacy. | Regressive | Macro-economic |
| | | Social inclusion | Social protection |
| | Strengthen the conditions that support higher wage growth, while respecting the role of the social partners. | Tackling inequality | Labour market |
| Improve educational outcomes and skills levels of disadvantaged groups. | Social investment – upskilling | Education | |

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| Greece Total no. 2 | Focus investment-related economic policy on sustainable transport and logistics, environmental protection, energy efficiency, renewable energy and interconnection projects, digital technologies, research and development, education, skills, employability, health, and the renewal of urban areas, taking into account regional disparities and the need to ensure social inclusion. | Social investment and inclusion | Social protection |
| | Achieve a sustainable economic recovery and tackle the excessive macroeconomic imbalances by continuing and completing reforms in line with the post-programme commitments given at the Eurogroup of 22 June 2018. | Regressive | Macro-economic |
| Hungary Total no. 4 | Continue the labour market integration of the most vulnerable groups in particular by upskilling, and improve the adequacy of social assistance and unemployment benefits. | Social inclusion | Labour Market |
| | Improve education outcomes and increase the participation of disadvantaged groups, in particular Roma in quality mainstream education. | Social investment – upskilling | Education |
| | Improve health outcomes by supporting preventive health measures and strengthening primary healthcare. | Tackling inequality | Social protection |
| | Ensure compliance with the Council recommendation of XX June 2019 with a view to correcting the significant deviation from the adjustment path towards the medium-term budgetary objective. | Regressive | Macro-economic |
| Ireland Total no. 5 | Achieve the medium-term budgetary objective in 2020. Use windfall gains to accelerate the reduction of the general government debt ratio. Limit the scope and number of tax expenditures, and broaden the tax base. Continue to address features of the tax system that may facilitate aggressive tax planning and focus in particular on outbound payments. | Regressive | Macro-economic |
| | Address the expected increase in age-related expenditure by making the healthcare system more cost-effective and by fully implementing pension reform plans. | Regressive | Macro-economic |
| | Provide personalised active integration support and facilitate upskilling, in particular for vulnerable groups and people living in households with low work intensity. | Social investment – activation | Labour market |
| | Increase access to affordable and quality childcare. | Social investment – upskilling | Labour market |
| | Focus investment-related economic policy on low carbon and energy transition, the reduction of greenhouse gas emissions, sustainable transport, water, digital infrastructure and affordable and social housing, taking into account regional disparities. | Social inclusion | Social protection |

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| Italy Total no. 8 | Ensure a nominal reduction of net primary government expenditure of 0.1% in 2020, corresponding to an annual structural adjustment of 0.6% of GDP. Use windfall gains to accelerate the reduction of the general government debt ratio. | Regressive | Macro-economic |
| | Shift taxation away from labour, including by reducing tax expenditure and reforming the outdated cadastral values. | Reconfiguration taxation mix | Taxation |
| | Fight tax evasion, especially in the form of omitted invoicing, including by strengthening the compulsory use of e-payments including through lower legal thresholds for cash payments. | Reconfiguration taxation mix | Taxation |
| | Implement fully past pension reforms to reduce the share of old-age pensions in public spending and create space for other social and growth-enhancing spending. | Regressive | Macro-economic |
| | Step up efforts to tackle undeclared work. | Social inclusion | Labour market |
| | Ensure that active labour market and social policies are effectively integrated and reach out notably to young people and vulnerable groups. | Social investment – activation | Labour market |
| | Support women's participation in the labour market through a comprehensive strategy, including through access to quality childcare and long-term care. | Social investment – activation | Labour market |
| | Improve educational outcomes, also through adequate and targeted investment, and foster upskilling, including by strengthening digital skills. | Social investment – upskilling | Labour market |
| Latvia Total no. 6 | Ensure that the nominal growth rate of net primary government expenditure does not exceed 3.5% in 2020, corresponding to an annual structural adjustment of 0.5% of GDP. | Regressive | Macro-economic |
| | Reduce taxation for low-income earners by shifting it to other sources, particularly capital and property, and by improving tax compliance. | Progressive | Taxation |
| | Address social exclusion notably by improving the adequacy of minimum income benefits, minimum old-age pensions and income support for people with disabilities. | Social inclusion | Social protection |
| | Increase the quality and efficiency of education and training in particular of low-skilled workers and jobseekers, including by strengthening the participation in vocational education and training and adult learning. | Social investment – upskilling | Education |
| | Increase the accessibility, quality and cost-effectiveness of the healthcare system. | Tackling inequality | Social protection |
| | Focus investment-related economic policy on innovation, provision of affordable housing, transport, notably on its sustainability, resource efficiency and energy efficiency, energy interconnections and on digital infrastructure, taking into account regional disparities. | Social inclusion | Social protection |

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| Lithuania Total no. 4 | Improve tax compliance and broaden the tax base to sources less detrimental to growth. | Reconfiguration taxation mix | Taxation |
| | Address income inequality, poverty and social exclusion, including by improving the design of the tax and benefit system. | Progressive | Taxation |
| | Improve quality and efficiency at all education and training levels, including adult learning. | Social investment – upskilling | Education |
| | Increase the quality, affordability and efficiency of the healthcare system. | Access | Social protection |
| Luxembourg Total no. 3 | Increase the employment rate of older workers by enhancing their employment opportunities and employability. | Social investment – activation | Labour market |
| | Improve the long-term sustainability of the pension system, including by further limiting early retirement. | Regressive | Macro-economic |
| | Address features of the tax system that may facilitate aggressive tax planning, in particular by means of outbound payments. | Increasing tax base | Taxation |
| Malta Total no. 3 | Ensure the fiscal sustainability of the healthcare and pension systems, including by restricting early retirement and adjusting the statutory retirement age in view of expected gains in life expectancy. | Regressive | Macro-economic |
| | Address features of the tax system that may facilitate aggressive tax planning by individuals. | Increasing tax base | Taxation |
| | Focus investment-related economic policy on research and innovation, natural resources management, resource and energy efficiency, sustainable transport, reducing traffic congestion and inclusive education and training. | Social investment – upskilling | Education |
| Netherlands Total no. 4 | Implement policies to increase household disposable income, including by strengthening the conditions that support wage growth, while respecting the role of social partners. | Tackling inequality | Taxation |
| | Address features of the tax system that may facilitate aggressive tax planning, in particular by means of outbound payments, notably by implementing the announced measures. | Increasing tax base | Taxation |
| | Reduce the incentives for the self-employed without employees, while promoting adequate social protection for the self-employed, and tackle bogus self-employment. | Tackling inequality | Labour market |
| | Strengthen comprehensive life-long learning and upgrade skills notably of those at the margins of the labour market and the inactive. | Social investment – activation | Labour Market |

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| Poland Total no. 4 | Ensure the adequacy of future pension benefits and the sustainability of the pension system by taking measures to increase the effective retirement age and by reforming the preferential pension schemes. | Regressive | Macro-economic |
| | | Social inclusion | Social protection |
| | Take steps to increase labour market participation, including by improving access to childcare and long-term care, and remove remaining obstacles to more permanent types of employment. | Social investment – activation | Labour Market |
| | Foster quality education and skills relevant to the labour market, especially through adult learning. | Social investment – activation | Education |
| | Ensure that the nominal growth rate of net primary government expenditure does not exceed 4.4% in 2020, corresponding to an annual structural adjustment of 0.6% of GDP. Take further steps to improve the efficiency of public spending, including by improving the budgetary process. | Regressive | Macro-economic |
| Portugal Total no. 5 | Adopt measures to address labour market segmentation. | Tackling inequality | Labour Market |
| | Improve the skills level of the population, in particular their digital literacy, including by making adult learning more relevant to the needs of the labour market. | Social investment – activation | Labour Market |
| | Increase the number of higher education graduates, particularly in science and information technology. | Social investment – upskilling | Education |
| | Improve the effectiveness and adequacy of the social safety net. | Social inclusion | Social protection |
| | Achieve the medium-term budgetary objective in 2020, taking into account the allowance linked to unusual events for which a temporary deviation is granted. Use windfall gains to accelerate the reduction of the general government debt ratio. Improve the quality of public finances by prioritising growth-enhancing spending while strengthening overall expenditure control, cost efficiency and adequate budgeting, with a focus in particular on a durable reduction of arrears in hospitals. Improve the financial sustainability of state-owned enterprises, while ensuring more timely, transparent and comprehensive monitoring. | Regressive | Macro-economic |

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| Romania Total no. 8 | Ensure compliance with the Council recommendation of XX June 2019 with a view to correcting the significant deviation from the adjustment path toward the medium-term budgetary objective. Ensure the full application of the fiscal framework. | Regressive | Macro-economic |
| | Strengthen tax compliance and collection. | Increasing tax base | Taxation |
| | Ensure the sustainability of the public pension system and the long-term viability of the second pillar pension funds. | Regressive | Macro-economic |
| | Improve the quality and inclusiveness of education, in particular for Roma and other disadvantaged groups. | Social investment – upskilling | Education |
| | Improve skills, including digital, notably by increasing the labour market relevance of vocational education and training and higher education. | Social investment – activation | Labour Market |
| | Increase the coverage and quality of social services and complete the minimum inclusion income reform. | Tackling inequality | Social protection |
| | Ensure minimum wage setting based on objective criteria, consistent with job creation and competitiveness. | Regressive | Labour Market |
| | Improve access to and cost-efficiency of healthcare, including through the shift to outpatient care. | Access | Social protection |
| Slovakia Total no. 4 | Achieve the medium-term budgetary objective in 2020. Safeguard the long-term sustainability of public finances, notably that of the healthcare and pension systems. | Regressive | Macro-economic |
| | Improve the quality and inclusiveness of education at all levels and foster skills. | Social investment – upskilling | Education |
| | Enhance access to affordable and quality childcare and long-term care. | Social investment – activation/upskilling | Education |
| | Promote integration of disadvantaged groups, in particular Roma. | Social inclusion | Social protection |
| Slovenia Total no. 3 | Achieve the medium-term budgetary objective in 2020. Adopt and implement reforms in healthcare and long-term care that ensure quality, accessibility and long-term fiscal sustainability. | Regressive | Macro-economic |
| | | Social inclusion | Social protection |
| | Ensure the long-term sustainability and adequacy of the pension system, including by adjusting the statutory retirement age and restricting early retirement. | Regressive | Macro-economic |
| | | Social inclusion | Social protection |
| Increase the employability of low-skilled and older workers by improving labour market relevance of education and training, lifelong learning and activation measures, including through better digital literacy. | Social investment – activation | Labour market | |

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|------------------------------|-------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|--------------------------------|-------------------|
| Spain Total no. 6 | Ensure that the nominal growth rate of net primary government expenditure does not exceed 0.9% in 2020, corresponding to an annual structural adjustment of 0.65% of GDP. Take measures to strengthen the fiscal and public procurement frameworks at all levels of government. Preserve the sustainability of the pension system. Use windfall gains to accelerate the reduction of the general government debt ratio. | Regressive | Macro-economic |
| | Ensure that employment and social services have the capacity to provide effective support. | Social investment – activation | Labour market |
| | Foster transitions towards open-ended contracts, including by simplifying the system of hiring incentives. | Tackling inequality | Labour market |
| | Improve support for families and address coverage gaps in national unemployment assistance and regional minimum income schemes. | Social inclusion | Social protection |
| | Reduce early school leaving and improve educational outcomes, taking into account regional disparities. | Social investment – upskilling | Education |
| | Increase cooperation between education and businesses with a view to improving the provision of labour market relevant skills and qualifications, in particular for information and communication technologies. | Social investment – activation | Education |
| Sweden Total no. 2 | Focus investment-related economic policy on education and skills, maintaining investment in sustainable transport to upgrade the different transport modes, in particular railways, and research and innovation, taking into account regional disparities. | Social investment – activation | Education |
| | Address risks related to high household debt by gradually reducing the tax deductibility of mortgage interest payments or increasing recurrent property taxes. | Reconfiguration taxation mix | Taxation |
| UK Total no. 2 | Ensure that the nominal growth rate of net primary government expenditure does not exceed 1.9% in 2020-2021, corresponding to an annual structural adjustment of 0.6% of GDP. | Regressive | Macro-economic |
| | Focus investment-related economic policy on research and innovation, housing, training and improving skills, sustainable transport and low carbon and energy transition, taking into account regional diversity. | Social investment – activation | Education |

ANNEX II

Table 1. List of social indicators currently used in the Semester

| POLICY AREA | INDICATOR | SOURCE |
|---------------|----------------------------------------------------------------------------------------------------------------|--------|
| Education | Early leavers from education and training (% of population aged 18-24) | JER |
| | Children aged less than 3 years old in formal childcare (%) | JER |
| | General government expenditure by function: education (% of GDP) | JER |
| | Adult participation in learning (% of population 25-64) | JER |
| | Tertiary education attainment (% of population 30-34) | JER |
| | Individuals who have basic or above basic overall digital skills (% of population aged 16-74) | JER |
| Labour market | Unemployment rate (% of active population aged 15-74) | JER |
| | Long-term unemployment rate (% of active population aged 15-74) | JER |
| | Employment rate (% of population aged 20-64) | JER |
| | Young NEET (Not in Education, Employment, or Training) (% of total population aged 15-24) | JER |
| | Gender employment gap (p.p.) | JER |
| | Gender gap in part-time employment (p.p.) | JER |
| | Gender pay gap in unadjusted form (% of average gross hourly earnings of men) | JER |
| | Activity rate (% of population 15-64) | JER |
| | Youth unemployment rate (% of labour force 15-24) | JER |
| | Employment in current job by duration (% of employed 20-64 from 0-11 months) | JER |
| | Transition rates from temporary to permanent contracts % (3-year average) | JER |
| | Employment rate of older workers (age group 55-64) | SPPM |
| | Labour productivity per hour worked (based on PPS per hour worked) | EPM |
| | Labour productivity per person employed (based on PPS per employed person) | EPM |
| | Temporary employees (% of total employees aged 15-64) | EPM |
| | Nominal unit labour cost growth (% change from previous year) | EPM |
| | Employment rate of low skilled persons (% of population with – at most – lower secondary education aged 20-64) | EPM |
| | Involuntary temporary employment (as % of total employees) | EPM |
| | Part-time employment (% of total employment aged 15-74) | EPM |
| | Inactivity and part-time work due to personal and family responsibilities (age 15-64) | EPM |

| | | |
|-------------------|---------------------------------------------------------------------------------------------------|------|
| Social Protection | Impact of social transfers (other than pensions) on poverty reduction (%) | JER |
| | Real adjusted gross disposable income of households per capita in PPS (2008 = 100) | JER |
| | Net earnings of a full-time single worker earning the average wage (PPS) | JER |
| | Income inequality – quintile share ratio (S80/S20) | JER |
| | At risk of poverty or social exclusion (AROPE) (in %) | JER |
| | Self-reported unmet need for medical care (%) | JER |
| | At-risk-of-poverty rate (AROP) (% of population) | JER |
| | Severe material deprivation rate (SMD) (% of population) | JER |
| | Persons living in a household with a very low work intensity (% of total population less than 60) | JER |
| | Severe housing deprivation (owner) (% of owners) | JER |
| | Severe housing deprivation (tenant) (% of tenants) | JER |
| | In-work-at-risk-of-poverty rate (AROP) (% of population) | JER |
| | General government expenditure by function: social protection (% of GDP) | JER |
| | General government expenditure by function: health (% of GDP) | JER |
| | Aggregate replacement ratio for pensions ratio | JER |
| | Healthy life years at age 65: women years | JER |
| | Healthy life years at age 65: men years | JER |
| | Out-of-pocket expenditure on healthcare (% of total health expenditure) | JER |
| | Median relative income of elderly people | SPPM |
| | At-risk-of-poverty (AROP) threshold for a single household | SPPM |
| | Persistent-at-risk-of-poverty (AROP) rate | SPPM |
| | At risk-of-poverty (AROP) rate for the population living in (quasi-)jobless households | SPPM |
| | Relative median at-risk-of-poverty gap | SPPM |
| | Children at risk of poverty or social exclusion | SPPM |
| | At-risk-of-poverty (AROP) rate of unemployed | EPM |

Source: own elaboration

Table 2. Headline Macroeconomic Imbalance Procedure (MIP) indicators and their threshold

| INDICATOR | THRESHOLD |
|---------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|------------------------------------------|
| 3-year backward moving average of the current account balance as % of GDP | +6% and -4% |
| Net international investment position as % of GDP | -35% |
| 5-year percentage change of export market shares measured in values | -6% |
| 3-year percentage change in nominal unit labour cost | +9% for €A MSs and +12% for non-€A MSs |
| 3-year percentage change of the real effective exchange rates based on Harmonized Index of Consumer Prices/ Consumer Price Index deflators, relative to 41 other industrial countries | ± 5% for €A MSs and ± 11% for non-€A MSs |
| Private sector debt (consolidated) in % of GDP | 133% |
| Private sector credit flow in % of GDP | 14% |
| Year-on-year changes in house prices relative to a Eurostat consumption deflator | 6% |
| General government sector debt in % of GDP | 60% |
| 3-year backward moving average of unemployment rate | 10% |
| Year-on-year changes in total financial sector liabilities | 16.5% |
| 3-year change in p.p. of the activity rate | -0.2% |
| 3-year change in p.p. of the long-term unemployment rate | +0.5% |
| 3-year change in p.p. of the youth unemployment rate | +2% |

Source: own elaboration

ANNEX III

A proposal of new indicators

J. Income inequality:

- ◆ Palma ratio⁴

K. Job-tenure insecurity, job quality and work representation:

a) Employment insecurity:

- ◆ Distribution of duration of employment with current employer by years in brackets (EU- Labour Force Survey) annual data
- ◆ Percentage of employees with a fixed-term contract (EU- Labour Force Survey) annual data
- ◆ Percentage of self-employed without employees of all persons in employment (EU- Labour Force Survey) annual data
- ◆ Percentage of employed persons expecting a possible loss of their job in the next 6 months (European Works Council-Eurofound). Data available: 2005, 2010, 2015
- ◆ Percentage of employed persons working for a temporary work agency (EU- Labour Force Survey) annual data
- ◆ Percentage of employees with a short-term contract of up to 3 months (EU- Labour Force Survey) annual data

b) Social dialogue:

- ◆ Trade union density rates, by employment status (Institutional Characteristics of Trade Unions, Wage Setting, State Interventions, Social Pacts Database)

- ◆ Percentage of employees being subject to a collective pay agreement (Structure of Earnings Survey-Eurostat) annual data

c) Working time and work-life balance: Labour Force Survey

- ◆ Percentage of employed persons who have more than one job, by labour status (EU- Labour Force Survey)
- ◆ Percentage of employed persons usually working 49 hours or more per week, per labour status (EU- Labour Force Survey)
- ◆ Percentage of employed persons usually working on Saturday or/ on Sunday, per labour status (EU- Labour Force Survey)
- ◆ Percentage of persons usually working at home by number of children, by labour status (EU- Labour Force Survey)
- ◆ Mean duration of one-way commuting time between work and home in minutes (European Working Conditions Surveys Eurofound). Data available: 2005, 2010, 2015

d) Job quality (autonomy, work intensity and work relationships):

- ◆ Percentage of employed persons having a good relationship with their colleagues (European Working Conditions Surveys-Eurofound). Data available: 2005, 2010, 2015
- ◆ Percentage of employees having a good relationship with their supervisor (European Working Conditions

⁴ The Palma ratio focuses on the differences between those in the top and bottom income brackets. The ratio takes the richest 10% of the population's share of gross national income (GNI) and divides it by the poorest 40% of the population's share. As explained in the text, this indicator better takes account of inequality, especially in a situation of progressive polarisation of income distribution. In this respect, the traditionally used GINI index is not very informative, because you can still have an improvement of the index, for instance, if the second top quintile becomes poorer other things being equal, while actually the situation has not improved.

Surveys Eurofound). Data available: 2005, 2010, 2015

- ◆ Percentage of employed persons exposed to employment-related physical, psychological or sexual violence in the last 12 months (European Working Conditions Surveys Eurofound). Data available: 2005, 2010, 2015
- ◆ Percentage of employees receiving regular feedback from their supervisor (European Working Conditions Surveys Eurofound). Data available: 2015
- ◆ Percentage of employed persons being able to choose their methods of work or to influence their pace of work (European Working Conditions Surveys Eurofound). Data available: 2005, 2010, 2015
- ◆ Percentage of employed persons thinking that they do useful work (European Working Conditions Surveys Eurofound). Data available: 2005, 2010, 2015
- ◆ Percentage of employed persons having to work at very high speed or to tight deadlines (European Working Conditions Surveys Eurofound). Data available: 2005, 2010, 2015
- ◆ Percentage of employed persons being able to influence decisions that affect their work (European Working Conditions Surveys Eurofound). Data available: 2005, 2010

L. Financial insecurity

- a) Household inability to meet an unexpected required expense, all households, percentage shares (Eurostat, EU- Statistics on Income and Living Conditions)

b) Household inability to meet an unexpected expense by households with or without dependent children, percentage shares (Eurostat, EU- Statistics on Income and Living Conditions)

c) Household inability to meet an unexpected expense, single person (male and female) household with dependent children, percentage shares (Eurostat, EU- Statistics on Income and Living Conditions)

d) Households that hold sight (current) and savings accounts, by labour status (European Central Bank Household Finance and Consumption Survey).

e) Median savings represented in monthly income equivalents (months), by labour status (European Central Bank Household Finance and Consumption Survey).

M. Equal opportunities in access to service (example for early childcare)

a) Share of children in childcare programmes, by household income decile and per hour of service (> 30 hours or < 30 hours) (EU- Statistics on Income and Living Conditions)

b) Age from which a place in early childcare facilities (e.g. kindergarten) is guaranteed (either legal right or compulsory participation)

c) Parental leave, by employment status

ANALYSIS ON THREE POLICY AREAS:

EMPLOYMENT & SOCIAL POLICIES



- 1 The current focus is on measuring disadvantage at the bottom of the income distribution
- 2 No attention is paid to the declining condition of intermediate segments of the population, i.e. the so-called "**squeezed middle**"
- 3 Indicators on job insecurity, financial insecurity and job tenure insecurity are missing
- 4 No attention is paid to the inequality of opportunities in social investment areas, e.g. **childcare and social services**

PUBLIC FINANCE & MACROECONOMIC POLICIES



- 1 There is a **persisting focus on budgetary stability and debt reduction**, which might have a regressive effect on inequality
- 2 The current Macroeconomic Imbalance Procedure (MIP) scoreboard **is devoid of macroeconomic indicators to measure inequality**
- 3 By setting tight constraints, the CSRs indirectly affect member states' capacity to use public resources to redistribute and conduct public investments

TAXATION POLICIES



- 1 Recommendations on personal income taxation are oriented toward the efficiency and productivity of the labour market and **disregard the redistributive potential of tax policy**
- 2 Tax matters identified as crucial in country reports do not appear consistently in the country-specific recommendations

RECOMMENDATIONS

- ✓ Include new indicators to: **capture the declining quality of work**, assess households' financial capability and measure income and wealth inequality.
- ✓ Integrate new indicators in the MIP to **monitor household financial fragility**; revise the expenditure rules of the Stability and Growth Pact; and **involve the social partners and wider civil society** in the process.
- ✓ **Encourage progressive taxation** consistently in country-specific recommendations; have **a coordinated approach to EU taxation dumping**; and expand the tax base in new areas, e.g. environment, in a progressive way

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Since its inception, the European Semester has attracted interest in its effects on EU's social outcomes. Nevertheless, the Semester is devoid of a framework to monitor socio-economic inequalities within member states.

In this policy study, Lorenza Antonucci and Francesco Corti propose a new framework to address the current Semester's limitations by: considering the rising socio-economic insecurity of the European lower-middle classes; connecting the social and economic aspects of the Semester; exploiting the redistributive effects of taxation. Accordingly, they develop a set of 9 recommendations for a new Semester that truly tackles inequalities.

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