Opinion on the Annual economic report for 1993

(93/C 108/08)

On 18 February 1993 the Council decided to consult the Economic and Social Committee, in accordance with Council Decision 90/141/EEC of 12 March 1990 on the attainment of progressive convergence of economic policies and performance during Stage One of Economic and Monetary Union, on the Annual economic report for 1993.

The Section for Economic, Financial and Monetary Questions, which was responsible for preparing the Committee's work on the subject, adopted its Opinion on 9 February 1993. The Rapporteur was Mr Vasco Cal.

At its 303rd Plenary Session (meeting of 24 February 1993), the Economic and Social Committee adopted the following Opinion by a majority vote with one abstention.

1. Introduction

1.1. The Commission approved its annual report on the economic situation in the Community on 3 February 1993. The Council Presidency wishes the ESC to draw up its Opinion by the end of February. This tight deadline has obviously hampered the organization of work and the drafting of the Opinion.

However, the importance and urgency of the matters considered in the report justify the ESC making an effort to reply and voice its views on time.

The Committee is also drawing up an Own-initiative Opinion on Growth and Employment.

1.2. At the Edinburgh Summit, the Conclusions of the Presidency included a Declaration on Promoting Economic Recovery in Europe, designed to 'reinforce the fundamentals of economic growth and encourage the creation of new jobs'.

1.2.1. Immediate measures were proposed by the European Council: in addition to the strengthening of the multilateral surveillance system, these included the establishment of a new, temporary lending facility of ECU 5 000 million within the European Investment Bank. This would be used to speed up the financing of capital infrastructure projects as part of the Trans-European Networks, and to set up a European Investment Fund with a capital of ECU 2 000 million (this figure should be considered in the light of the ECU 1 000 000 million spent annually on investment in the EC).

2. The economic situation, its causes and prospects, as viewed by the Commission

2.1. The annual economic report sees no possibility of economic trends altering in the short term, and considers that it is only in the medium term that the Community has the chance of attaining its growth potential of around 3 % per year once more.

2.2. The macro-economic material included in the report can no longer hide the gravity of the economic situation facing the Community.

2.2.1. Community Gross Domestic Product (GDP) rose by over 3 % during the period 1988-1990. However since then, contrary to forecasts and expectations, growth in Community GDP has become so sluggish that the rate for 1991-1993 as a whole is no higher than the rate for each year between 1988 and 1990.

2.2.2. Gross fixed capital formation in the Community, after growing at an annual rate of around 7 % between 1987 and 1989, fell to 3,8 % in 1990, 0,5 % in 1991, and 1 % in 1992. The forecast for 1993 is now negative (− 0,5 %). The trend in investment in equipment is even worse.

2.2.3. The EC average for inflation has remained since 1989 at around 5 % per year (since 1989 the private consumption deflator has stood at 4,9 %, 4,5 %, 5,3 % and 4,6 %, with 4,6 % forecast again for 1993). Over the same period the US rate has fallen from 5 % in 1989/1990 to around 3 % in 1992/1993, while in Japan it has remained at between 2 and 3 % per year.

2.2.4. The main factor behind the Community's worsening trade deficit has been the decline in the German trade surplus since 1989.

The balance on current transactions, as a percentage of GDP, has moved from parity in 1989 to deficit: − 0,3 % in 1990 and − 1 % in 1991 and 1992, with a forecast of − 1 % again for 1993.

2.2.5. Member States' budgetary situations continued to diverge from the targets laid down in the

protocol appended to the Maastricht Treaty; general government net borrowing in the Community as a whole, as a percentage of GDP, rose from 2,9 % in 1989 to 4,1 % in 1990, 4,6 % in 1991, and 5,3 % in 1992, with a forecast of 5,75 % for 1993.

2.2.6. Total employment in the EC rose by 1,5 % in 1989/1990, causing a drop in unemployment to 8,3 % at the end of 1990. However, in 1991 employment grew by only 0,1 % and in 1992 it contracted by 0,5 %. A fall of 0,8 % is forecast for 1993. This would mean an unemployment rate of 11 %—the equivalent of 15 million unemployed—in 1993.

Capacity utilization in manufacturing industry, which stood at around 85 % in 1990, fell to 82 % in 1991 and was below 80 % in 1992.

2.2.7. The annual increase in real compensation per employee (applying the private consumption deflator) fell from 2,8 % in 1990 to 1,8 % in 1991 and 1,3 % in 1992; for 1993, no increase is forecast.

The profitability of fixed capital continued to rise until 1990/1991, nearing the historic levels of the period 1961-1973.

2.3. The reasons put forward by the Commission to explain such a serious deterioration in the economic situation over the last few years, and the inaccuracy of successive forecasts, are as follows:

2.3.1. the economic cycle: a period of 'abnormal' above-potential growth in 1988/1989 fuelled inflationary pressures that had to be corrected (in terms of both wages and budgets) by means of a tighter monetary policy from 1989/1990;

2.3.2. developments in the United States (where GDP rose by 0,7 % in 1990 and fell by 1,3 % in 1992) and Japan (where growth slackened from 5,2 % in 1990 to 4,4 % in 1991 and 1,5 % in 1992), together with the exchange rate of the dollar, which must have caused problems for EC exporters;

2.3.3. German unification, which initially stimulated domestic demand (5 % per year in 1990/1991) but then led to imbalances (higher inflation than usual, budget deficit of around 3,5 % of GDP, not to mention factors which remain outside the budget but which will be included from 1995 onwards);

2.3.4. speculation on the money markets during the summer of 1992, causing the Pound Sterling and the Lira to leave the Exchange Rate Mechanism and the most vulnerable currencies (Peseta, Escudo, Irish Punt) to be devalued;

2.3.5. the political situation in all Member States, which worsened after the Danish and the French referenda, creating a climate of uncertainty about progress in Political Union and Economic and Monetary Union;

2.3.6. lastly, the combination of the above factors which has steadily eroded consumer and business confidence since 1989, reaching all time lows at the end of 1992.

2.4. The Commission is not very optimistic about the economic outlook for 1993. It sees no alternative to the present economic and financial policy, which it considers must be continued.

2.4.1. As regards the conditions laid down in the Maastricht Treaty, the Commission considers it necessary to reaffirm Member States' commitment to the goals for nominal convergence targets in order to create the climate for a healthy economic recovery and help boost business and consumer confidence.

2.4.2. In the Commission's view, the main short-term problems remain inflationary pressures, budgetary consolidation, and wage moderation (notably in the public sector). It feels that if any of these were to get out of control they could jeopardize the conditions for higher Community growth from 1995/1996.

3. Comments on the economic situation and the measures needed

3.1. The nominal convergence criteria laid down in the Maastricht Treaty must be seen as medium-term criteria for paving the way towards non-inflationary growth and the establishment of the Economic and Monetary Union (EMU). They must now be flanked by a stronger real growth target, without which the deterioration in the economic situation and unemployment could jeopardize the economic and social cohesion and steady improvement in living standards enshrined in Article 2 of the Treaty.

3.2. The growth and employment initiative decided by the Heads of State and Government is to be welcomed, as it recognizes the gravity of the situation and its adverse effects on unemployment, and makes growth and job creation the priority concern of Community policy.

However, given the seriousness of the economic situation, one might have expected swifter and more effective decisions, so that the general public could feel the impact of the action decided at EC level.

3.3. The growth and employment initiative must be backed by concerted action in the field of international economic relations, so as to curb rising protectionist

pressures and secure an international climate conducive to the Community growth strategy.

3.4. The growth and employment strategy must not be put at risk by restrictive budgetary policies which could hamper economic growth. Whilst respecting the targets for nominal convergence in the medium-term, urgent steps are nevertheless needed to re-launch growth.

Inflation rates have to be reduced if the EC is to withstand world competition and regain its competitiveness worldwide.

3.5. Community coordination must be stepped up. The economic measures to be taken by the Member States under the growth and employment initiative must be coordinated and announced at Community level, and must not simply reflect domestic contingencies.

3.6. The conflicts between domestic and external economic policy objectives in some European countries must be clarified and resolved as rapidly as possible, particularly where they concern the maintenance of currency parities, the erosion of competitiveness, budget deficits and public sector debts.

3.6.1. The Committee recommends that there should be a renewed commitment to common, coordinated and timely action by all Member States in relation to exchange rates.

3.7. Real interest rates, particularly short-term rates, are at one of the highest levels ever in the developed world as a whole. As the Organization for Economic Cooperation and Development (OECD) recognizes in its latest annual report (December 1992), high interest rates have hampered growth in Europe. Although falling inflation in most Member States has led to a drop in deposit rates, lending rates have not followed suit.

3.7.1. However, a distinction has to be made between short-term rates, which are directly influenced by the action of the Central Banks, and long-term rates, which depend mainly on the balance between savings and investment, and above all, on expectations for inflation.

3.7.2. In Germany, for example, the long-term deposit rate is currently around 0,3 % below the American rate, while its short-term rate is around 5,4 % lower.

It is to be hoped that the Bundesbank's recent decision to cut the Lombard rate by 0,5 % and the discount rate by 0,25 % will trigger a generalized cut in the cost of money in Europe.

3.7.3. A cut in interest rates is the way to create the conditions for a rise in investment and private consumption, and for reducing public debt burdens.

3.7.4. The implicit interest rate on the debt is higher than the nominal GDP growth rate (comprising growth in real terms and price increases, both of which are slackening). This has had a snowball effect and worsened debt levels, despite the improvement in the primary budget balance of countries striving to reinforce budgetary discipline.

3.8. In recent years the financial institutions in many OECD countries have shown a preference for property loans, since property assets appeared to offer sound guarantees for the loans granted.

3.8.1. As the increased competition was not always matched by proper monitoring of the credit institutions, it led to an explosion in property prices, which these institutions felt reinforced those guarantees.

3.8.2. Property prices then collapsed in a number of countries, triggering bankruptcies and calling for large injections of public funds. More generally, the quality of the assets was called into question.

3.8.3. The gravity of the situation is having serious consequences—which need to be carefully assessed—on the rate of economic recovery. This is acknowledged to be slower and weaker than at similar periods in the past.

3.8.4. Current debt levels (household, corporate, public sector) are such that a fall in interest rates alone will not be enough to inject greater momentum into the economy. Measures are also needed to make more efficient and productive use of capital, so that lending is channelled into productive investment rather than speculative projects in the property sector, for example.

3.9. Infrastructure investment, notably on the Trans-European networks in the transport, energy and telecommunications sectors, now comes under Community responsibility following the inclusion of a new Title in the Treaty, designed to ensure that the single market is of real benefit.

3.9.1. Preparatory work on the projects (many of which have already been identified) should be speeded up, and both the Member States and the EC authorities

should state now which projects could begin ahead of schedule.

3.9.2. The Cohesion Fund should also be brought into force as soon as possible.

3.9.3. In addition to the direct effects of these decisions on a sector which is being seriously hit by the present recession, an earlier start on the work would demonstrate the commitment to, and confidence in, economic recovery.

3.10. The annual economic report makes no mention of the macroeconomic effects of the decisions taken at the Edinburgh Summit concerning the Community's financial perspective up to the year 1999, including the increase in the Structural Funds, but these should be included among the factors likely to encourage recovery.

3.10.1. Although the perspective approved is less ambitious than the Commission's initial proposals, the own resources ceiling has been raised, the Structural Funds have been given a significant boost, and increases in commitments for internal policy and external action (notably vis-à-vis Central and Eastern Europe) are also guaranteed.

3.10.2. In total, the Community budget will rise from approximately ECU 70 000 million in 1993 to around ECU 84 000 million in 1999; of the latter sum, ECU 30 000 million will go to structural measures.

3.10.3. The important direct and indirect effects of these transfers on beneficiary countries, as well as the increased demand on suppliers in other Member States, will undoubtedly play a major part in creating a climate of confidence, particularly as the existence of a multi-annual framework will avoid the uncertainties generated by annual budgets.

Done at Brussels, 24 February 1993.

3.11. The role of the social partners and their contribution to ending the present recession has been an abiding feature of Community documents since it was realized that the economic situation had got far worse than expected.

3.11.1. The social partners are asked to exercise pay restraint, this being considered a prerequisite for financial stability. They are also called upon to accept labour market flexibility, in order to increase employers' readiness to take on new workers.

On the subject of pay trends, the Commission also specifies that only half the increase in productivity should go on rises in real wages. The other half should be used to boost profitability.

3.11.2. Less attention has been paid to the social partners' requests to the Community decision-making bodies, notably in the statement adopted on 3 July 1992 under the Community Social Dialogue procedure; these requests concern the need for a more dynamic economic policy, a cut in interest rates, an increase in investment and monetary stability and the creation of lasting jobs.

3.11.3. Greater worker participation in corporate decisions (for example regarding the improvement of working methods, the introduction of new technologies and innovations in production processes), is vital if the European economy's competitiveness is to be restored and reinforced over the long term. The delays in modernizing labour relations in some Member States are one of the reasons for the serious shortage of skilled labour and for firms being unable to meet their requirements, at a time of high unemployment (the other main reason is the inadequacy of vocational training systems, which do not meet companies' real needs).

The Chairman

of the Economic and Social Committee

Susanne TIEMANN