ECONOMIC OUTLOOK

OCTOBER 2002

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The UNICE Economic Outlook provides a business insight into recent economic developments, based on a survey of UNICE member federations in the 15 member states of the EU. The main purpose of the publication is to provide a clear picture of the current business climate in Europe, and the trends that emerge.

Qualitative data and forecasts were established in September 2002. Aggregate values are GDP (at PPS) weighted, unless otherwise indicated.

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Table 1: UNICE forecasts

EU-12	**2002**	**2003**
GDP (annual % change)	0.9	2.1
Inflation (%)	2.2	1.9
Unemployment (%)	8.3	8.2
Employee Compensation (annual % change)	3.2	3.0
EU-15	**2002**	**2003**
GDP (annual % change)	1.0	2.2
Inflation (%)	2.1	2.0
Unemployment (%)	7.7	7.6
Employee Compensation (annual % change)	3.3	3.4

EXECUTIVE SUMMARY

Whatever happened to recovery?

The economic recovery in Europe is stalling. While at the beginning of the year, cautious optimism seemed appropriate, recent developments have shown that the European economy has not pulled itself out of the mud, yet. UNICE is now expecting economic growth in the EU to remain below 1% this year. Recovery is still expected for 2003, however, although European business reckons it will be weaker than previously thought, as there is a general lack of economic activity throughout Europe.

Or will things change for the worse?

UNICE now expects a more drawn-out recovery than six months ago… all fingers crossed. As serious downside risks threaten the world economy, things could easily become worse. The scenario of a Europe plunging back into recession cannot be ruled out and has even become likelier during the last weeks. The United States – the most important stimulus for the European economy this year - is not immune to a worsening of its economic situation given its high levels of household and corporate debt, and ever-worrying current account imbalance. Markets watch nervously over the possibility of a conflict with Iraq. Investment decisions are postponed. Energy prices have already climbed considerably this year, and fears persist of a veritable oil price shock should the situation in the Middle East escalate. Stock markets have gazed into the abyss, lately, and there is no guarantee that share prices' race for the bottom is over, given the bad financial situation of companies and rising risks of default for bonds and loans.

A stuttering European growth motor

But even assuming that no major economic downward shocks occur – as UNICE does in this Economic Outlook -, the European growth motor is stuttering. Most of its fuel has come from outside the EU, this year. But since growth forecasts have also been slashed in the United States, the EU can rely less and less on a recovery driven by export demand. Order books are weak, and will not be filled by persistently anaemic domestic demand. Consumer confidence is being driven down by the uncertain international climate and high unemployment rates, which remain a heavy burden for the whole society. Current growth rates in the EU are not sufficient to create jobs, given the levels of labour productivity and wages. Therefore labour costs must be lowered in order to make it interesting for employers to hire new staff. Wage demands at rates in line with or above productivity growth levels would be counterproductive in such circumstances. In spite of economic slowdown, high wages and energy prices have moved inflation to levels uncomfortable enough for the ECB to be on guard, leaving it with little room for manoeuvre in monetary policy.

What is to be done?

Confidence must be restored in the European economy. Policy-makers throughout the EU must prove that they still have their budgets under control. The recent doubts having been raised regarding the commitment of several large countries in the Euro-zone towards budget discipline have sent the wrong signals to the markets. The downward business cycle should not serve as an excuse for running deficits. UNICE urges the Member States to respect their commitments within the Stability and Growth Pact. Sound public finances are essential for a healthy European economy, especially if it is to be prepared for the ageing population challenge.

Furthermore, structural weaknesses and rigidities must finally be tackled throughout the EU. Policy-makers must send clear signals that they are still determined to create the most dynamic and competitive economy in the world. Today's highly turbulent economic environment needs entrepreneurs, investors and employees to act quickly and adapt flexibly to changes in market conditions. Especially the labour market must be liberalised throughout the EU, in order to drive down unemployment, which in turn will restore consumer confidence and provide a badly needed stimulus for economic growth. Experience with easing up the labour market in several Member States has proven to be very positive.

UNICE makes its forecasts in this Economic Outlook under the assumption that no major downward risks will occur in the international environment. Yet the world economy is facing risks, which could cause serious negative economic shocks.

One big question mark has become the development of the business cycle in the US whose current recovery is linked to aggressive policy measures boosting demand such as a large increase in defence expenditure. American consumer spending has remained strong thanks to, among other things, a zero-rate financing policy in the car sector and a refinancing of mortgages (housing wealth effect). But households will not be able to keep that level of spending forever. The US recovery has not yet seen any important increase either in national income or in employment.

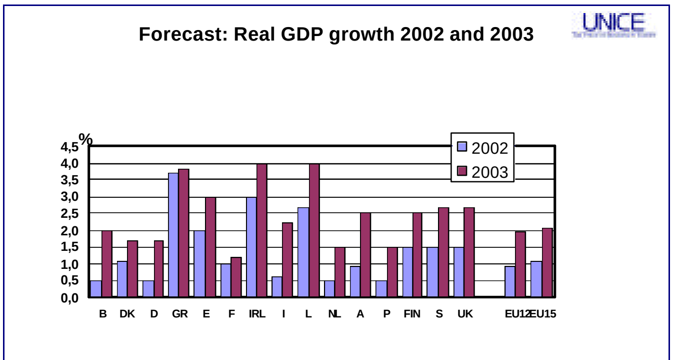
Furthermore, markets watch nervously over the possibility of a conflict with Iraq. Energy prices have already climbed considerably this year, and fears persist of a veritable oil price shock should the situation in the Middle East escalate. Stock markets have plunged lately, and there is no guarantee that share prices' race for the bottom is over, given the bad financial situation of companies and rising risks of default for bonds and loans.

Therefore, UNICE cannot fully exclude a double-dip recession even though it is not expecting it.

FORECASTS

In this year's second Economic Outlook UNICE has again revised its growth forecasts downwards.

Chart 1



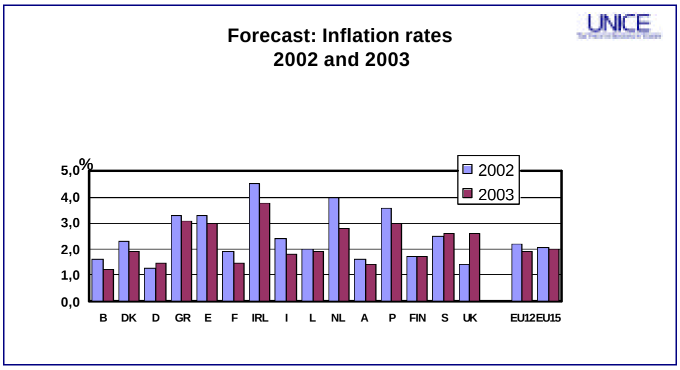
For the current year 2002 UNICE predicts that the economy in EU-12 (the members of the Euro-zone) will only have grown by 0.9%. The growth rate in EU-15 (plus Denmark, Sweden and the UK) is expected to be 1.0%. Six months ago, growth forecast by European business for 2002 was still at 1.2% for EU-12 and 1.3% for EU-15. The only country with an upward growth revision for 2002 is Denmark.

But growth rates are very diverse among Member States. Like six months ago, Greece, Ireland and Luxembourg stand out with expected growth rates of around 3% or more for 2002 and 2003.
France, Spain, Austria, Finland, Denmark, Sweden and the UK range in the midfield with growth rates of between 0.9% and 2%, whereas Germany, the Netherlands, Belgium and Portugal now expect growth of merely 0.5%. The Netherlands has revised its growth forecast downwards to one third, from 1.5% to 0.5%. Italy is now also expected to grow very slowly with a growth forecast revised from 1.3% to 0.6% for 2002.

Under the assumption that no major economic shocks will occur, UNICE is still expecting recovery for next year, although it is going to be weaker than previously thought. In 2003 growth rates are expected to be 2% on average in the EU-12 (2.1% in EU-15). Almost all countries have revised their estimates for 2003 downwards, as well. Only Spain, Austria and the UK have left their forecasts unchanged.

Inflation in the Euro-zone is expected to remain around the 2% target fixed by the ECB.

Chart 2



However, compared with the figures six months ago, expected inflation for 2002 has been revised upwards from 1.7% to 2.2% on average (from 1.7% to 2.1% in

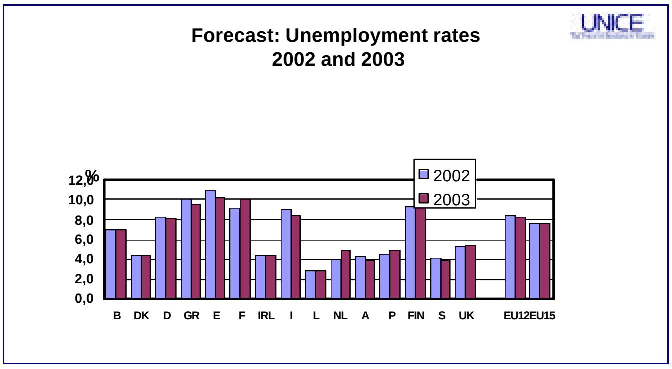
EU-15). This is mainly due to considerable upward revisions in France and Italy, but Greece, Spain, the Netherlands, Portugal, Denmark, Sweden and Ireland have also revised their forecasts upwards. Given that growth forecasts have mainly been cut, this is remarkable and has its main causes in the persistently high oil price this year as well as in high wage rises.

In 2003 inflation is expected to stay just below 2% in EU-12 (and exactly 2% in EU-15) provided that there are no further price shocks like, for example, oil and food price shocks or excessive wage increases. Six months ago, inflation projections for 2003 were at 1.7% and 1.9% respectively.

Unemployment will remain at high levels - and has even been revised slightly upwards for 2002 in EU-12. It is now expected to be 8.3% in 2002 (7.7% in EU-15). With almost the same rates predicted for 2003 (8.3% in EU-12, 7.6% in EU-15) no relief is expected in the near future. Under the current economic conditions no new jobs will be created in the EU.

But, again, the rates vary enormously among Member States.

Chart 3



Whereas in Greece, Spain and Italy, the relatively high unemployment rate is expected to fall perceptively in 2003, the Dutch unemployment rate is expected to rise from 4% in 2002 to 5% in 2003. Business equally expects the French unemployment to rise considerably from 9.2% in 2002 to 10% in 2003. As will be seen below, the positive employment developments can be chiefly explained by measures to inject flexibility into the labour market, whereas in the Netherlands the fear of high wage rises is the cause of the pessimistic outlook for employment.

ECONOMIC CLIMATE

European business is concerned about slackening economic growth. While at the beginning of the year the economy was mostly felt to be on the recovery track, business sentiment now has become more negative, again.

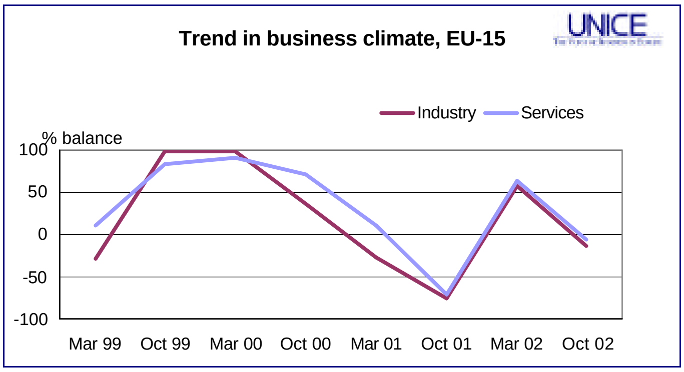
The balance of expectations – the share of weighted replies expecting an improvement in the business climate in the next six months, compared with the share expecting a deterioration – has even fallen back below zero for both industry and services in the EU-15.

More than 40% of weighted replies expect a negative trend in business climate for industry as well as for the service sector in EU-15. In EU-12 this share amounts to more than 50%. In contrast, the share of weighted answers expecting positive developments remains around 30% for both industry and services. Of these 30%, Italy, Belgium and Spain (or 27% of weighted replies) predict a positive trend but add that it will be only a weak one.

The negative feeling is not surprising given the general lack of activity in the European economy.

Export demand from the United States, by far the biggest force pushing the business cycle upwards earlier this year, has become weaker as recovery in the world's biggest economy is postponed.

Chart 4



This chart as well as charts 4,5,6,7,14 and 17 shows the difference between weighted shares of respondents expecting positive developments over the next six months and those expecting negative developments. Changes in this balance can be followed at six-monthly intervals from March 1999, when this survey was first carried out, to October 2002, giving an indication of the trend.

Hence order books will be weak. Help from elsewhere is not in sight, least of all from notoriously weak domestic demand. In addition, stocks were built up in the first half of 2002 and are now being run down, so there is not much incentive for production. It cannot be excluded that manufacturing output will actually contract, if economic activity does not pick up. In some countries, exceptions to this trend can be found in the chemical, pharmaceutical, timber and food sectors, as well as in the construction sector in the UK and Spain. On the other hand, in Germany the automobile, machinery, equipment and electronic sectors are doing worse than average. In Italy, where an overall positive business climate is expected, the textile industry is reckoned to remain negative.

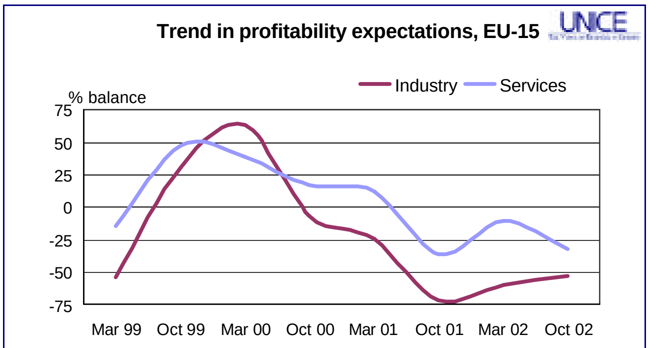
In services retail is doing well in the UK, mainly driven by very rapid growth in spending, which might soon come to an end, however. After its gold rush, the ICT-sector is still struggling throughout Europe. Greece and Spain are worried about the performance of the tourism sector.

PROFITABILITY

Given the current economic conditions it is hard for companies to make profits. Especially in the industrial sector, more than two thirds (72% in the EU-15, 70% in the EU-12) of weighted replies hold lower profitability expectations than six months ago. For services the prevailing mood is that of unimproved profitability conditions – 60% in the EU-15 and 70% in the EU-12 expect profitability for services to remain the same.

The balance chart underlines this overall negative feeling towards the profitability trend. Negative expectations outweigh positive ones.

Chart 5



In fact, profit margins are being squeezed from both sides. International prices are further deteriorating and, at the same time, production costs are rising.

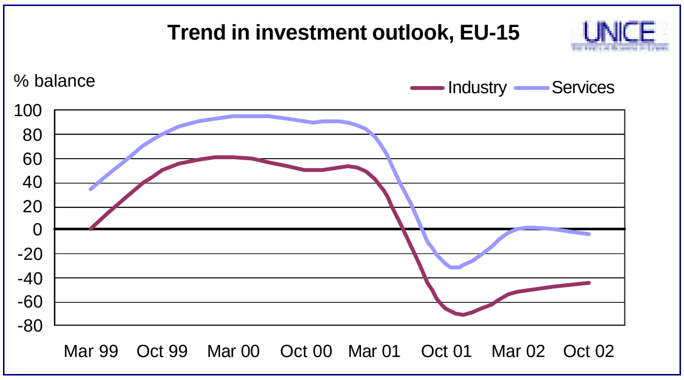
World prices are particularly low in the industrial sector, which is more dependent on the business cycle than services. With the recent Euro appreciation, export prices have come under further pressure. On the cost side, business will have to cope with higher unit labour costs, as well as rising energy prices (although this is somewhat alleviated by the Euro appreciation) and insurance costs.
Continuously low capacity utilisation also weighs on profitability as overcapacities can often not be driven down in time.

Exceptions to these gloomy prospects are rare. In EU-12 only Italy expects a (very slight) positive profitability trend for its industry sector. Outside the Euro-zone, Denmark and Sweden have positive profitability expectations due to higher demand from abroad.

INVESTMENT

Investment prospects mirror profitability prospects. Like six months ago, investment is on hold. On weighted average it is not expected to pick up, with sentiment for industry being worse than sentiment for services.

Chart 6



For industry over two thirds (69% in EU-12, 70% in EU-15) report negative investment intentions over the next six months.

For services the dominant feeling is that of unchanged investment prospects. About half of weighted replies say that the overall investment climate will change neither for the better nor for the worse (54% in EU-12, 54% in EU-15). That said, it should be kept in mind that the ICT sector particularly will have to continue its dis-investment measures to tackle overcapacity problems following the investment boom in these sectors in the late 1990s.

With subdued sales expectations and narrow margins driving down corporate profits, the currently low capacity utilisation rate is not projected to improve in the near future. Therefore it is unlikely that many companies in Europe will make major investment decisions.

Furthermore, in Germany and France a deterioration of financing conditions can be observed. Although real interest rates are low, banks have become more careful in granting loans as the economic future becomes riskier.

Especially in the Scandinavian countries an on-going decline can be observed in third-generation-telecom- and other ICT-investments.

On the other hand, in Italy the so-called Tremonti-bis law, which provides fiscal incentives to invest should positively affect investment in both industry and service sectors. However, the more sectors are dependent on export demand, the more hesitant their investment plans will be.

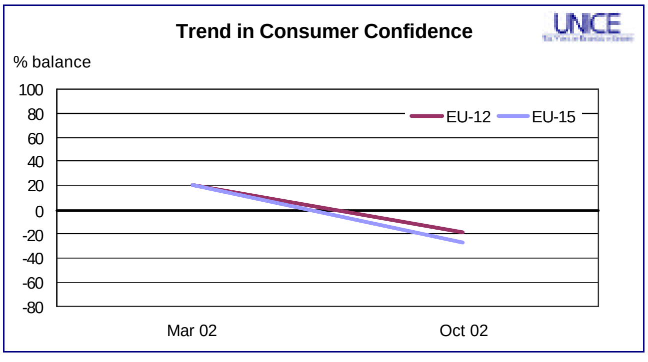
In Spain fixed investment could pick up again, given the past decline.

CONSUMER CONFIDENCE

Since the March 2002 Economic Outlook UNICE has been questioning its member federations on the expected development in consumer confidence.

Consumer confidence in the EU has been at disturbing lows ever since the beginning of 2002. Now the weighted balance of consumer confidence has become even worse than six months ago and has slipped below zero, i.e. negative expectations (56% in EU-12, 61% in EU-15) are dominant. Furthermore, member federations expecting consumer confidence to develop positively (37% in the EU-12, 33% in the EU-15) stress the fact that the absolute level of consumer confidence will remain low.

Chart 7



The EU is going through a consumer confidence crisis, of which one major cause is the employment situation. If many Europeans continue to be worried about finding or keeping a job, consumer confidence is unlikely to pick up.

Furthermore, the recent tumble in European and global share prices has further disturbed the confidence of many Europeans who joined in the “new equity culture” a couple of years ago, investing in shares for the first time and who are now experiencing wealth impairment. Fears about a possible escalation of the political crisis in the Middle East might also play a role in restricting consumer demand.

Relatively low inflation rates should contribute to more favourable conditions for consumption. However, *perception* of inflation seems to be higher. Contrary to statistical evidence, many consumers in the Euro-area believe that, due to the introduction of Euro notes and coins, prices of frequently bought products have been rounded up, giving them the feeling of being worse off.

In the UK, consumer demand has been stronger than in most other EU countries. This is likely to change, however, as income growth will be slower than in previous years, employment prospects flat at best and tax rises are in the pipeline; furthermore, doubts about individual financial positions, given high debt levels, have recently increased.

In Ireland, consumer confidence is further dampened by the belief that the period of exceptional growth rates is over.

FINANCIAL MARKETS

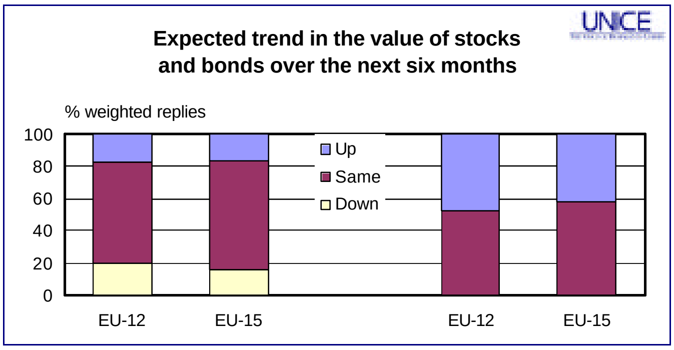
In the past weeks and months fears of a war against Iraq, gloomy prospects for the world economy and shrinking corporate profits have taken their toll on global share prices. European stock markets have been among the most deeply affected.

Uncertainty has been growing among UNICE member federations regarding the development of share prices. 68% of weighted replies in EU-15 do not commit themselves to either upward or downward predictions for highly volatile stock prices.

The share of replies finding the current decline in stock prices exaggerated and thinking it likely that an upward correction will take place has fallen from 43% (38% in the EU-15) in March 2002 to merely 18% (16% in the EU-15) at present.

In times of uncertainty, risk free government bonds are a safer haven for savings than stocks. They are less apt to fall, a scenario expected by no UNICE member federation. 48% in EU-12 and 42% in EU-15 think that bond prices will tend to go up in the coming months.
In Germany possible higher budget deficits might cause an upward trend in bond yields.

Chart 8



Business, consumer and investor confidence are all very low and not certain to pick up in the next six months. What was seen as the beginning of a recovery in the first half of this year, stemmed mainly from export demand, which is set to falter, if conditions in the US deteriorate.

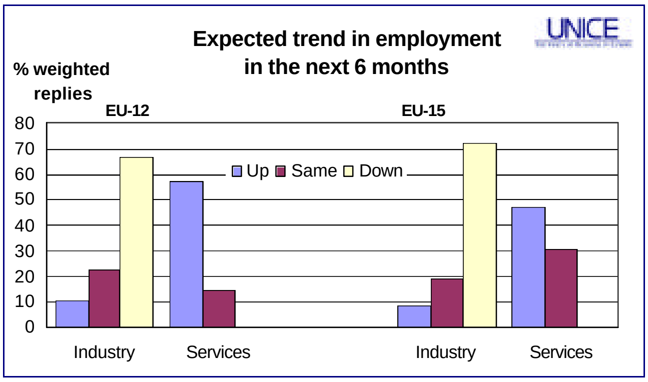
As room for manoeuvre in monetary policy is extremely limited and fiscal policy must above all tackle structural deficits, the only way in which policy-makers can send signals to restore confidence without destabilising the economy is through structural reforms. Further liberalisation of labour, product and financial markets would improve the EU's growth potential and restore confidence in times of uncertainty.

LABOUR MARKET AND WAGE INDICATORS

EMPLOYMENT

Given the current levels of labour productivity and wages in the EU, the growth rates expected in the EU will not suffice to create more jobs.
UNICE data suggest that employment might actually decrease in the next six months; there are fears that further lay-offs will be necessary in order to drive down overcapacity. Especially in the industrial sector, employment is projected to fall.

Chart 9



In industry, 67% of weighted replies in EU-12 (72% in EU-15) expect employment to go down. The service sector, less sensitive to the business cycle, could experience some positive development as 57% of weighted replies in EU-12 (47% in EU-15) are expecting employment to go up. Taking into account that the unemployment rate is not expected to change much for the better on average in the EU in 2002 and 2003, positive developments will be compensated by negative developments.

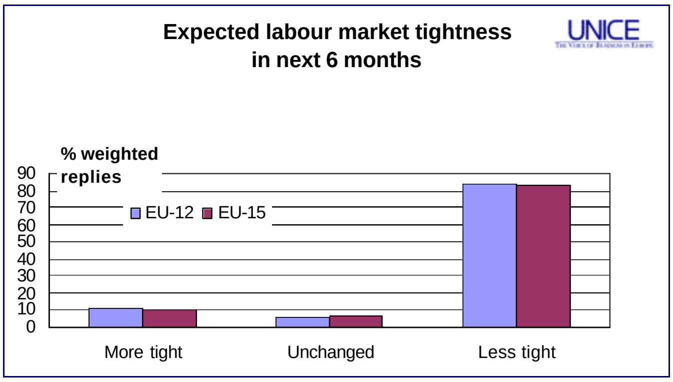
With growth rates too low to create jobs, positive developments in employment must be achieved through liberalisation measures in rigid labour markets. In Italy, for example, incoming deregulation measures (experimental three-year lay-off regulation for SMEs, part-time regulation and introduction of more flexible labour contracts for new employees) will probably have a positive impact on the employment rate, if the opposition of unions does not dilute their implementation.

Spain has been a positive example of job creation for the past few years through labour flexibilisation measures. Upcoming reforms could be delayed, however, which would risk negative effects on the employment situation and make the labour market tighter.

On the other hand, Germany, which is expecting to have continued lay-offs in the industrial as well as the service sectors, still badly needs to undertake liberalisation measures in the labour market. The announced reforms proposed by the Hartz-Commission will not be sufficient to provide the German labour market with the necessary flexibility.

As for expected labour market tightness in the EU, the UNICE data give a clear picture: more than 80% of weighted responses in EU-12 as well as in EU-15 anticipate that the labour market will be less tight in the upcoming six months.

Chart 10



These figures should not dilute the fact, however, that labour markets in Europe remain remarkably tight, given the overall high level of unemployment rates in Europe. There is still a shortage of certain skills. Although rising or stagnating unemployment rates will ease that situation, the core problems of labour market tightness are structural: demand for human capital is often not matched by available supply on the labour market.

The UK labour market is currently very tight and, with a more and more protracted economic recovery now expected, there could be some easing in the labour market. However, some specific sectors may suffer from competition with the public sector, as the UK government undertakes a recruitment drive.
Denmark is particularly concerned about growing tightness on the labour market.

LABOUR PRODUCTIVITY AND LABOUR COST

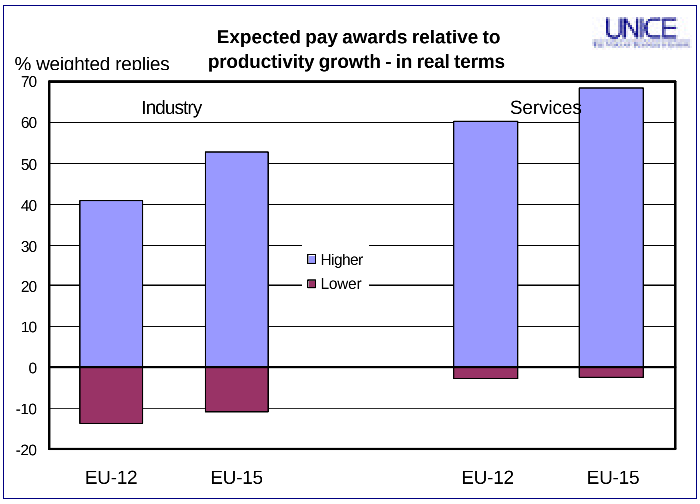
Labour productivity will remain at low levels in the EU as output is low and lay-offs reducing overcapacity often occur after a certain delay. The lag in liberalisation in key service sectors such as energy, transport or postal services is adding to low productivity levels as the organisational structures of enterprises in these sectors remain inefficient. The number of working hours per person is low compared to the EU's main competitors.

84% of weighted replies consider labour productivity growth in industry to be low (83% in EU-15). For services, the corresponding figure is 37% (46% in EU-15). If this trend in labour productivity prevails, the long-term growth potential of the European economy will be seriously hampered. There are laudable exceptions to this trend, e.g. in the Irish chemical industry, where productivity growth is much higher than average.

In order to make it profitable for companies to hire new staff in the current situation of low growth, the increase in labour cost must be below productivity growth. However, the opposite is the case. A large majority of replies fears that wage increases alone will be higher or equal to productivity growth. Only in Luxemburg, Portugal and Spain (and there only for the industrial sector) wage increases are expected to be lower.

In addition to the fact that excessive wage increases will not help the unemployed, they lead to more inflation and thereby risk worsening the monetary conditions for recovery. Wage increases that claim to "compensate" for inflation merely trigger a wage-price spiral. Examples of wage increases leading to higher inflation can be observed Italy and the Netherlands.

Chart 11



Employment prospects continue to be gloomy. UNICE has repeatedly urged policy-makers finally to undertake the necessary labour market reforms that enable the reallocation of human capital where it is needed. The labour laws in many Member States are simply not yet fit for today's more dynamic economy. The countries that went furthest in liberalising their labour markets have the lowest levels of unemployment, e.g. Denmark and the UK. Even modest reforms bear fruit, as is currently demonstrated by Italy.

Furthermore, in times of limping economic growth, wage increases should remain lower than the rise in labour productivity in order for the economy to create jobs at the current modest growth rates. Excessive wage increases only make matters worse by causing inflation and damaging employment prospects. Policy-makers must countersteer the current developments in labour cost, otherwise jobs will be killed in the EU instead of being created.

FINANCIAL AND MONETARY ASPECTS

APPROPRIATENESS OF MONETARY POLICY

The ECB has not altered interest rates since the last Economic Outlook was published. But compared with six months ago, when a considerable portion of member federations considered the monetary policy of the ECB too tight, now a large majority (72% of weighted replies in the EU-15) finds it appropriate.

This reflects the tendency in the economic environment for higher inflation. Especially the jump in oil prices and the level of actual and expected wage increases have created inflationary pressure above the 2% target set by the ECB, in spite of stagnation in economic growth. Core inflation (leaving out more volatile prices like food and energy) was even estimated at 2.5% by the ECB in the middle of this year.

Chart 12

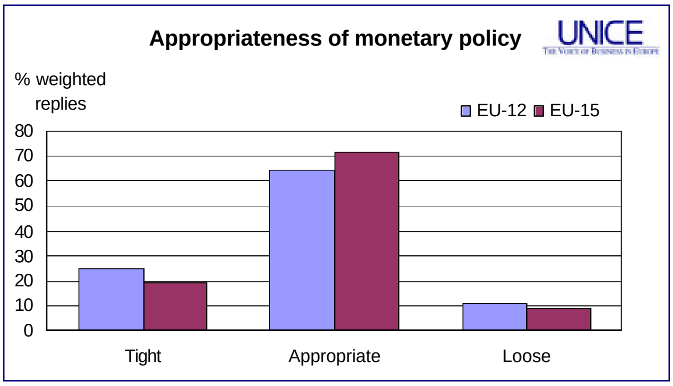
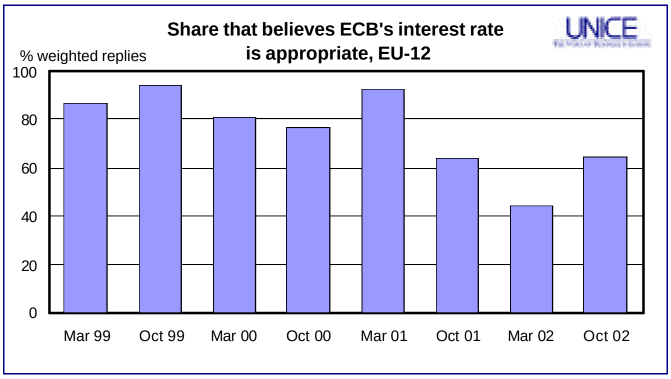


Chart 13



A further limitation on ECB's room for manoeuvre is caused by the recent doubts about the commitment of several large Member States to maintain fiscal discipline. The inadequate policy-mix of several governments leads to imbalances in the Euro zone. Not all governments have adjusted their economic policy to the single European currency.

The overall opinion of the ECB remains largely positive (74% in EU-12 and 60% in EU-15).

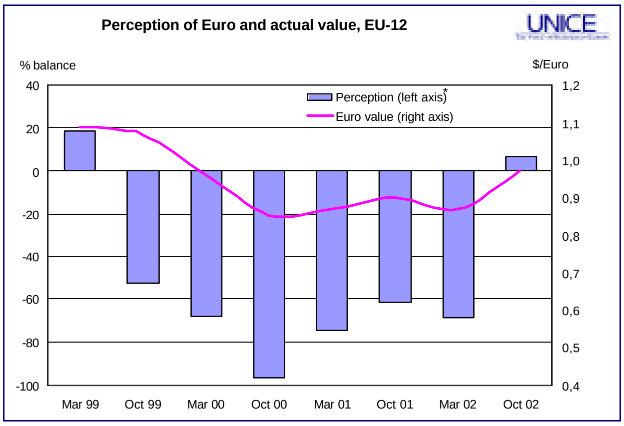
THE VALUE OF THE EURO AND ITS PERCEPTION

In the past six months, the value of the Euro compared with the Dollar has increased. Hence it is not surprising that a smaller share of countries (16% in EU-12) now consider the Euro undervalued (compared with 68% in March).

On the other hand it is important to point out that only a relatively small share of weighted replies (22% in the EU-12) perceives the Euro as overvalued as against the Dollar. 61% see the current value of the Euro as appropriate.

It is understood, that the increase of the Dollar/Euro exchange rate has certainly made conditions for export not any easier. Nevertheless, the Euro appreciation seems to be in line with fundamentals. Besides it has eased the recent increase in energy prices.

Chart 14



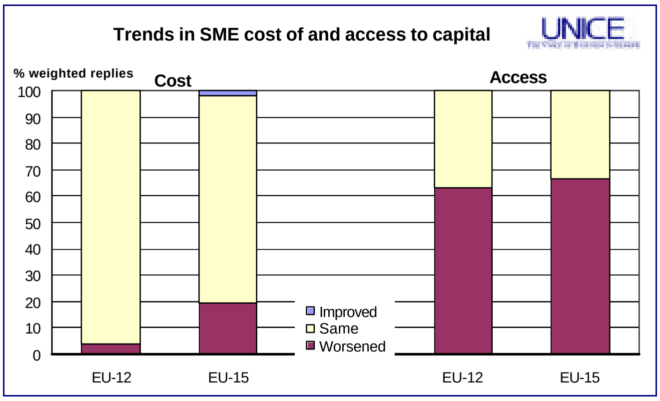
** Perception of the Euro is the difference between weighted shares of respondents who think the Euro value against the Dollar is too high and those who think it is too low. The 61% of weighted replies perceiving the Euro value as appropriate are not included in the chart.*

COST OF AND ACCESS TO CAPITAL FOR SMES

Costs for SMEs to raise capital have, on the whole, stayed the same. Only in Belgium and the UK are SMEs facing higher costs than six months ago.

On the other hand, over 60% of weighted replies find that access to capital for SMEs has become more difficult. In Germany, France, Austria, the Netherlands, Finland and the UK, a more restrictive lending policy by banks can be observed. This is taking account of the increased risks in the corporate sector.

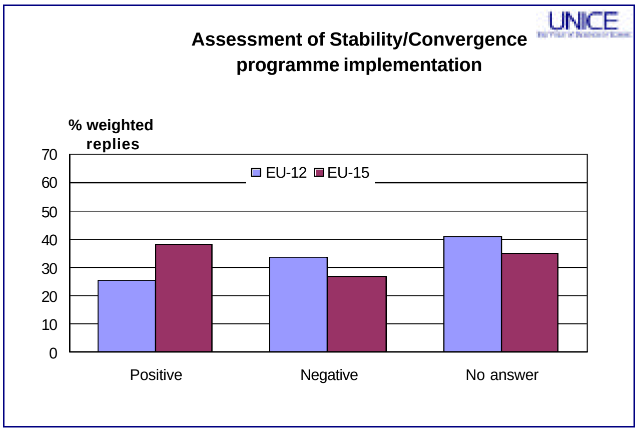
Chart 15



BUDGETARY POLICY IN MEMBER STATES

In the UNICE evaluation of fiscal policy, two groups of member states emerge: the group of countries which have succeeded in getting their budgets under control, and those who are still struggling with the level of their deficits. The latter group comprises Germany, Italy, France and Portugal. Although small in number, these Member States together make up more than half of the EU's GDP.

Chart 16



Germany faces heavy reform pressure as its budget deficit might well exceed 3% this year. The commitment to reach a balanced budget in the medium term will be challenged by the low growth rates in its economy, which could considerably lower its prospected tax revenues. The newly elected government will now have to take painful measures, as it failed to decide on the right steps while economic conditions were still more favourable. Currently, German economic activity is subdued by financial policy, as it must cope with increasingly high tax burdens and social security contributions.

In France great uncertainty remains about how and when budgetary balance can be achieved. The French government must undertake serious fiscal reforms, if it is to keep its deficit under control. The French business federation estimates that under current economic circumstances this year's budget deficit will approach 3% and reach 3.5% in 2003.

The Italian Government has recently presented an update to the Document for Economic and Financial Planning laying out the provisions for 2002. The GDP growth has been lowered from 1.3% to 0.6% and net deficit in percentage of GDP has been raised from 1.1% to 2.1%. The update takes into account above all the relevant decrease of the incomes in the last seven months.

In the Financial Law presented on 30 September (still not approved as the Economic Outlook went to the printers) the Government itself forecast a deficit/GDP ratio for 2003 equal to 1.5%.

Portugal has started putting in place an austerity programme, which receives a positive evaluation from Portuguese business. However, there are still doubts about whether budget balance will be achieved over the medium term.

Out of the group of Member States with essentially sound public finances, the following receive some criticism from business federations regarding their budget policy:

The Finnish budget receives negative evaluations by its business and employers' federations. They are concerned about the easing of budget discipline in view of the parliamentary elections in March 2003, and particularly fear that the government might not commit itself to structural income tax reductions. However, the general government surplus in Finland is still more than 2% despite of the slowdown in economic growth.

Austrian business warns its government of tendencies to increase the budget deficit, and voices growing concern about achieving balance over the medium term.

Irish business also urges its government to control the current spending growth. There is large spending pressure, especially associated with public sector wages and essential infrastructure that might threaten budget balance over the economic cycle.

Swedish business finds it likely, too, that the balanced budget will not hold. In next year's budget, a deficit of 1 to 2 % is possible.

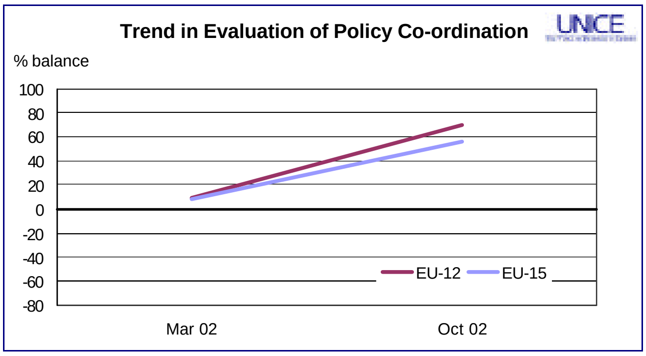
In the Netherlands, the newly elected government has decided to increase the tax burden next year considerably - mainly for employees - a measure designed to counterbalance the deteriorating budgetary position. In view of the sluggish, below-potential growth of the Dutch economy, the strong increase in the tax burden may serve as an extra brake on the recovery of the Dutch economy. The timing of this tax increase, which will be followed by reductions in later years, does not seem optimal.

Greek business appreciates the overall positive direction of fiscal policy but demands more ambitious efforts in bringing down the high debt burden.

In view of weaker than expected economic growth, many governments will have to take into account falling tax revenues in their budget planning. Policy coordination at the EU level helps Member States to manage their public finances in times of mounting pressure. The overall feeling of UNICE member federations towards EU policy coordination is positive (83% of weighted replies in the EU-12, 69% in the EU-15) and has increased over the last six months.

Although it is felt that coordination mechanisms could be improved, they have put pressure on national governments to consolidate public finances. Public finances are now analysed more openly. However, different speeds in structural reforms persist, and the coordination will be harmed if lax budget behaviour, especially of the larger member states, holds sway.

Chart 17

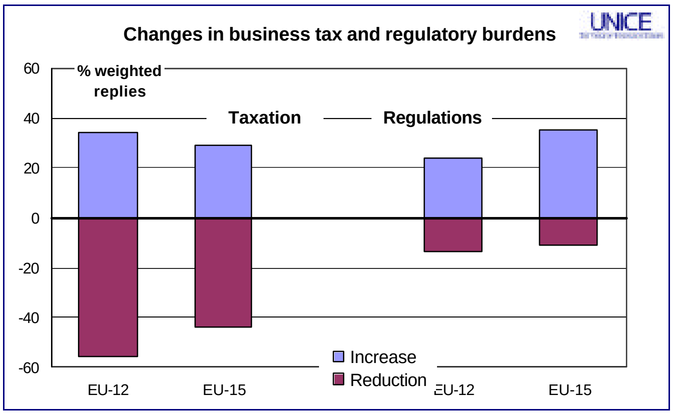


TAX AND REGULATORY BURDEN

Levels of regulations have not changed tremendously in the past months. In Spain and Austria, business feels that regulation has decreased, whereas Belgium is experiencing an increase in regulation as a result of strict environmental policies starting to be implemented. The UK points at a raft of regulation, for example in the employment field. France has also suffered from increased regulatory measures in the past but there is hope of relief, especially concerning the 35-hour week.

Irish business has mixed feelings about newly implemented regulation measures: the Protection Act for part-time workers has brought more exhaustive application criteria for work permits. On the other hand, the new Competition Act receives a positive assessment as it makes the permission for mergers dependent on the question of whether or not a merger substantially reduces competition. Changes in commercial transactions regulations encourage companies to pay debts on time.

Chart 18



As for taxes, several countries are undertaking or will undertake efforts to decrease the tax burden on companies:
In Italy companies are making use of investment incentives. In the new financial law, the Italian Government has decided to enact tax cuts that will take effect already in 2003, as agreed in the “Pact for Italy” signed last July by the Government, the trade unions and the business community. In particular, cuts in personal income tax will benefit lower-income households. It is planned to make up the resulting reduction in tax revenue by the proceeds of various measures to bring the grey economy into the tax net. Thus, the total disposable income might remain unchanged. Corporate tax is being lowered from the current 36% to 35%, while certain tax benefits provided for by law have been slightly reduced, as well as investment incentives for businesses. Business associations have expressed deep concerns over these cuts, which could have negative effects on growth, especially in Southern Italy. All in all, firms could face an increase in the tax burden although changes in taxation are still under revision.

Irish business has benefited from a reduced corporation tax for services as well as from a reduction in social welfare contributions. It expects further reduction of the corporate tax rate for services but an increase for new manufacturing.

The tax burden has decreased in Luxembourg (tax reform for companies in 2002), Greece (tax incentives for mergers and for new job offers) and Finland (decrease in employers' social security contributions).

In Belgium a decrease in tax charges is expected to take account of the decline in the corporate tax rate from January 2003 onwards. In Spain a business tax reform, albeit mild, will also take place in 2003. France is awaiting the fiscal reform of its new government.

Germany is worried about postponements of planned tax reductions. An increase in corporate tax rates will occur in the next six months in order to finance the damage caused by the flooding.

In the Netherlands, the tax burden has slightly decreased, mainly through lower social premiums and a small reduction in the rate of company taxation. On the other hand, business is expecting a limited increase in the tax burden from January 2003 onwards (see chapter: Budgetary policy in Member States).

MAIN RISKS OVER THE NEXT SIX MONTHS

As pointed out at the beginning of this Economic Outlook, the international environment is facing risks which could cause negative economic shocks and seriously endanger recovery in the EU. Risks of a further oil price hike in the wake of a military confrontation in the Middle East that gets out of hands or the risk of a US double-dip recession pose considerable threats to the world economy. New terrorist attacks could shake confidence in overall political stability. But especially the risk of a financial crisis in the wake of the recent fall in share prices throughout the world has become more imminent since data for this Economic Outlook were established in September 2002.

Alongside these major downside risks in the international environment, UNICE member federations also mention risks within the EU:

- Many see the economic situation in the big countries as a major potential threat to the whole of Europe.
- Political risks must be taken into account in Ireland, where a rejection of the Nice Treaty in the Referendum could delay political reform in the EU and isolate Ireland, and in Austria, where due to early elections, there are fears of political instability.
- If the potential problems connected with enlargement are not duly solved, it is felt that this will worsen the EU's political and financial situation. However, if the remaining problems are solved and the new member states are smoothly integrated, enlargement is expected to result in an increase in investment activity.
- Possible high levels of wage increases are also perceived as a big threat in numerous Member States because they would cause inflation to soar and worsen the employment situation.
- Another EU-specific concern that was once more explicitly mentioned by many member federations in this October 2002 survey is the risk of general failure of the Lisbon Strategy to increase EU competitiveness.

LIST OF UNICE MEMBER FEDERATIONS SURVEYED IN THE ECONOMIC OUTLOOK

BDI	Germany
CBI	UK
CEOE	Spain
CIP/AIP	Portugal
CONFINDUSTRIA	Italy
DI	Denmark
FEDIL	Luxembourg
FGI	Greece
IBEC	Ireland
MEDEF	France
SVENSKT NARINGSLIV	Sweden
TT/PT	Finland
VBO-FEB	Belgium
VNO-NCW	Netherlands
VOI	Austria

October 2002 UNICE Economic Outlook

	B	D	GR	E	F	IRL	I	L	NL	A	P	FIN	EU-12	DK	S	UK	EU-15
Forecasts 2002																	
Real GDP (annual % growth)	0,5	0,5	3,7	2,0	1,0	3,0	0,6	2,7	0,5	0,9	0,5	1,5	0,9	1,1	1,5	1,5	1,0
Inflation (%)	1,6	1,3	3,3	3,3	1,9	4,5	2,4	2,0	4,0	1,6	3,6	1,7	2,2	2,3	2,5	1,4	2,1
Unemployment (%)	6,9	8,3	10,0	11,0	9,2	4,5	9,0	2,8	4,0	4,2	4,6	9,3	8,3	4,4	4,1	5,3	7,7
Nom. compensn of employees (annual % growth)													3,2				3,3
Forecasts 2003																	
Real GDP (annual % growth)	2,0	1,7	3,8	3,0	1,2	4,0	2,2	4,0	1,5	2,5	1,5	2,5	2,0	1,7	2,7	2,7	2,1
Inflation (%)	1,2	1,5	3,1	3,0	1,5	3,8	1,8	1,9	2,8	1,4	3,0	1,7	1,9	1,9	2,6	2,6	2,0
Unemployment (%)	7,0	8,2	9,5	10,2	10,0	4,3	8,4	2,8	5,0	3,9	5,0	9,3	8,3	4,3	3,8	5,4	7,6
Nom. compensn of employees (annual % growth)													3,0				3,4
Question 1	**Trend in business climate over the next 6 months**												Ind/Ser				Ind/Ser
positive	Ser			Ind Ser		Ser	Ind Ser					Ind Ser	32 37	Ind Ser	Ind Ser		30 34
negative		Ind Ser	Ser		Ind Ser			Ind Ser	Ind				55 51				43 41
neither pos nor neg	Ind		Ind			Ind			Ser	Ind Ser	Ind Ser		13 12			Ind Ser	27 26
Question 2	**Trend in profitability over the next 6 months**												Ind/Ser				Ind/Ser
positive							Ind						20 0	Ind Ser	Ind Ser		20 4
negative	Ind	Ind	Ind	Ind	Ind Ser	Ind Ser		Ind Ser			Ind Ser		70 24			Ind Ser	72 36
unchanged	Ser	Ser	Ser	Ser			Ser		Ind Ser	Ind Ser		Ind Ser	11 76				9 60
Question 3	**Trend in investment over the next 6 months**												Ind/Ser				Ind/Ser
positive				Ind Ser			Ind Ser	Ind					31 30	Ind Ser			26 26
negative	Ind Ser	Ind	Ind		Ind	Ser		Ser	Ind Ser	Ind	Ind Ser	Ind Ser	68 16			Ind Ser	70 29
unchanged		Ser	Ser		Ser	Ind				Ser			2 54		Ind Ser		4 45
Question 4	**Level of exchange rate with**												H/A/L				H/A/L
USD	Low	Appr	High	Low	High	Low	Appr	Appr	Appr	Appr	Appr	Appr	22/61/16	Appr	Low	Appr	18/67/15
GBP	Low	Appr	High	Low	na	Low	Appr	Appr	Low	Low	Appr	High	4/50/25	Appr	Low	na	3/42/22
JPY	Appr	Appr	na	Low	na	Low	Appr	Appr	Appr	Appr	Appr	Appr	65/12/78	Appr	High	Appr	2/70/10
Euro	Appr	na	na	na	na	na	na	na	na	na	na	na		Appr	Low	High	
others: SEK	na	na	High	na	na	na	na	na	na	na	na	Low		na	na	na	
Question 5	**Stance of monetary policy**																
tight					yes					yes		yes	25				20
appropriate	yes	yes	yes			yes	yes	yes	yes		yes		65	yes	yes	yes	72
loose				yes									11				9
Question 6	**What is your opinion of the ECB (conduct of monetary policy favourable to business, transparency)**																
positive	yes	yes	yes	yes			yes	yes	yes		yes		74	yes			60
negative										yes			3			yes	19
no answers					yes	yes						yes	23		yes		21
Question 7	**Compared to 6 months ago, SME's cost/access to capital for business development is**												C A				C A
higher / more difficult	C A	A			A				A	A		A	4 63			C A	20 66
same		C	C A	C A	C	C A	C A	C A	C	C	C A	C	96 37	A	C A		79 34
lower / less difficult													0 0	C			2 0
Question 8	**Trend in government bonds yields and stock market prices over the next 6 months**												U/S/D				U/S/D
Stock mkt prices	up	same	same	up	down	same	same	same	same	up	same	same	18/63/20	same	up	same	16/68/16
Govt bond yields	same	up	same	same	same	same	up	same	same	same	same	same	48/52/0	up	up	same	42/58/0

	B	D	GR	E	F	IRL	I	L	NL	A	P	FIN	EU-12	DK	S	UK	EU-15
Question 9	**Trend of total tax burden on business in the past 6 months**																
increased					yes								20				16
decreased			yes			yes	yes	yes	yes				30				24
unchanged	yes	yes		yes						yes	yes	yes	50	yes	yes	yes	60
Question 10	**Trend in total tax burden on business in the next 6 months**																
increase		yes							yes				34	yes			29
decrease	yes			yes	yes	yes	yes						56				44
no change			yes					yes		yes	yes	yes	10		yes	yes	27
Question 11	**What is your assessment of the budgetary policy programme for 2002?**																
positive	yes			yes	yes			yes			yes		37	yes			31
negative		yes								yes		yes	33		yes	yes	45
no answer			yes			yes	yes		yes				30				24
Question 12	**Implementation of the Stability & Growth Pact: what is your assessment of your country's multinannual stability programme?**																
positive	yes		yes	yes				yes	yes			yes	25	yes		yes	38
negative		yes								yes	yes		34				27
no answer					yes	yes	yes						41		yes		35
Question 13	**Regulations that harm competitiveness have increased, decreased or not changed?**																
Increase	yes				yes								24			yes	35
No change		yes	yes			yes	yes	yes	yes		yes	yes	63	yes	yes		54
Decrease				yes						yes			14				11
Question 14	**Overall trend in employment**												U/S/D				U/S/D
Ind: past 6 mnths	Down	Down	Same	Down	Down	Down	Up	Same	Down	Down	Down	Down	20/3/78	Down	Down	Down	16/2/82
Ind: next 6 mnths	Down	Down	Same	Up	Down	Down	Same	Same	Down	Down	Down	Down	11/22/67	Same	Down	Down	9/19/72
Ser: past 6 mnths	Same	Down	Up	Down	Up	Up	Up	Down	Same	Down	Same	Up	45/12/42	Down	Same	Up	52/12/35
Ser: next 6 mnths	Same	Down	Up	Up	Up	Up	Up	Same	Same	Up	Same	Same	57/15/28	Up	Same	Same	47/30/23
Question 15	**Expectation of labour markets over the next 6 months**																
more tight				yes									11	yes			10
unchanged			yes					yes			yes		5		yes		7
less tight	yes	yes			yes	yes	yes		yes	yes		yes	84			yes	83
Question 16	**Evaluation of labour productivity**												Ind/Ser				Ind/Ser
high	Ind												4 0				3 0
average		Ser	Ind Ser	Ser		Ind Ser		Ser	Ind			Ind	12 43	Ind Ser	Ind Ser		14 39
low	Ser	Ind		Ind	Ind Ser		Ind Ser	Ind	Ser	Ind Ser	Ind Ser	Ser	84 57			Ind Ser	83 61
Question 17	**Wage growth compared with productivity growth:**												Ind/Ser				Ind/Ser
higher	Ind Ser	Ind Ser	Ind Ser				Ser		Ind Ser				41 60	Ind Ser	Ind Ser	Ind Ser	53 68
same				Ser	Ind Ser	Ind Ser	Ind			Ind Ser		Ind Ser	46 37				36 29
lower				Ind				Ind Ser			Ind Ser		14 3				11 2
One-off questions																	
A	**Will public finances achieve balance (or a surplus) over the medium-run/the economic cycle?**																
Yes	yes			yes			yes	yes	yes			yes	42	yes			35
No		no	no		no	no				no			55		no	no	63
no answer											no ans		2				2
B	**Has policy co-ordination at the EU level improved the national management of public finances?**																
Yes	yes	yes	yes		yes	yes	yes		yes			yes	83		yes		69
No				no						no			14	no			13
no answer								no ans			no ans		3			no ans	19
C	**How will consumer confidence develop over the next 6 months?**																
Positively				pos			pos		pos				37	pos	pos		33
Negatively	neg	neg			neg	neg					neg		56			neg	61
no answer			no ans					no ans		no ans		no ans	7				6