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SPEECH

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Address by UNICE President Ernest-Antoine Seillière
Macroeconomic Dialogue at Political Level

The recovery in the euro area seems to be on a firmer footing than expected only a few months ago, even considering the stagnation of French GDP in the third quarter, which was compensated by positive outcomes in most other countries.

In this context, UNICE revised its forecasts for growth in 2006 and 2007 upwards by ½% from the Spring. Growth in the euro area is estimated to reach 2.5% in 2006 and 2.0% in 2007.

On the domestic side, investment and job creation are gaining strength, which bodes well for the future. But there are a number of challenges that need to be addressed to make this recovery sustainable.

Firstly: there is still a long way towards sustainable public finances

The current improvement in the euro area fiscal position is mainly due to excessive deficit countries moving back towards the 3% limit, which I recall is not a target but a ceiling.

We have two problems with current fiscal developments:

- The consolidation strategy of excessive deficit countries is mainly based on increased taxation rather than spending restraints
- Other countries show limited interest in taking new measures in a stronger growth environment.

With demographic pressures building-up, insufficient consolidation will have three negative effects on the current recovery:

- It will raise expectations of more painful adjustments in the future
- It will weaken the central bank's capacity to deliver low interest rates
- It will contribute to maintain cyclical divergences within the euro area. With a single monetary policy, fiscal policies become the main instrument to avoid persistent periods of overheating and overcooling at the national level.

We therefore ask the Eurogroup to take steps and:

- Exert more pressure on countries to use good times to their deficits more rapidly
- Set concrete deadlines for Member States to reach their medium-term budgetary objectives

Secondly: no sustained recovery is achievable without a productivity revival

Despite the current cyclical upturn, UNICE estimates in its latest Economic Outlook report that labour productivity growth per hour worked will remain below 1½% this year and next, in line with the poor average performance of the last decade.

This is a major factor hampering income prospects and our capacity to face the challenges ahead, including demographic ageing.

There is nothing inevitable about this situation. Europe can have both employment and productivity growth. In fact, it will need both to sustain its social model in the future. But this will not come without further reforms.

I would like to say "en passant" that there is clearly a link to be made between the flexicurity debate and the productivity challenge in Europe. In the context of the EU Social Dialogue, UNICE is currently emphasising this link, as social partners try to build a common understanding of the main labour market challenges.

The recent Commission Green Paper on Labour Law is contributing to this debate, but we regret that it is largely influenced by an outdated perception of a conflict between labour market flexibility and security for workers. In today's labour market, security is primarily about acquiring the necessary skills and adapting to new opportunities. It is not about strict employment protection rules which hamper the creation and growth of new business and decrease the speed of adjustment to changes.

The responsibility for reforms lies primarily with the Member States, but EU institutions play an important role as well, especially in the period running up to the Spring European Council. In this context, we look forward to the Commission's Progress Report to be published on 12 December and hope to see clear commitments to fill the reform gap by all stakeholders.

In this exercise of multilateral surveillance of reform progress, we expect the Eurogroup also to take responsibility, reflecting the strong policy interactions that exist in monetary union and the specific challenges that are associated with them.

Thirdly: wage developments must be consistent with productivity trends

Business is not calling for the lowest possible wage outcome. But to ensure sustained growth over the years ahead it is important that wage developments remain:

- Aligned with productivity trends, including across sectors and various segments of the labour market
- Responsive to the aim of restoring competitiveness, particularly in those countries which have accumulated significant imbalances in recent years

These conditions are essential to ensure that the recovery consolidates both internally, with strong employment growth, and externally, with increased competitiveness supporting exports and investment.

At present, our baseline scenario is for wage growth to remain contained over the next two years, and in this regard, should not be viewed as a reason for the ECB to hike interest rates further.

Finally, the ECB should take fully into account the risks of euro appreciation

The current monetary policy stance of the ECB is considered appropriate, and the business community supports its emphasis on solidly anchoring inflation expectations at a low level.

This is particularly important in the euro area because structural rigidities make prices and wages adjust very slowly. This implies that letting inflation overshoot has worse consequences for future growth and jobs than in a more competitive economy.

That said, our national business federations also tell us that insufficient attention is given to exchange rate risks.

We are worried that in the context of widening global current account imbalances, the ECB could involuntarily trigger a damaging appreciation of the euro by prolonging its tightening cycle.

If a decision to raise interest rates is taken in December, we call on the ECB to pause afterwards, especially considering the improved inflation outlook after the recent drop in oil prices.

Europe is experiencing a recovery but the momentum remains fragile. As usual in an upswing, structural difficulties seem less pressing and the temptation to delay necessary measures is rising.

These have been the mistakes of the past, and I hope that this time all policy stakeholders will live up to their responsibilities in order to sustain the recovery over the years ahead.

I am looking forward to a fruitful debate on how macroeconomic policies can best contribute to this objective and how they must complement and reinforce the reform momentum.

Thank you for your attention

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