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SPEECH

*** Check against delivery ***

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Speech by Philippe de Buck, Director General of BUSINESSEUROPE

Dear Mr. Rotowski, President Juncker, President Trichet,
Commissioner Rehn, Ladies and Gentlemen,

When I addressed this forum the last time, in February this year, the upturn of the economy had been stronger than expected. The recovery was initially driven by exports, which stimulated industrial production and company investment. This, in turn, translated into higher employment and consumption, and the recovery broadened to the domestic sector.

Investments and net exports have accounted for almost 60% of total economic growth in the EU since the beginning of 2010. The fact that Europe was able to “export its way out” of the crisis shows the need of Europe to remain competitive in the world stage. It also underscores the importance of facilitating businesses activity as an engine of wealth creation in the society.

Nevertheless, and despite that the recovery was becoming increasingly self-sustained, instability in financial markets associated to political uncertainty, feeding through business and consumer sentiment, has started to take a toll on the real economy. Investments and exports started to lose steam, and private consumption became negative in the second quarter.

The economic situation has worsened substantially during the summer due to political inability to stop the contagion of the sovereign debt crisis, and the outlook for the second half of the year has been downgraded substantially. Economic sentiment and overall business climate have deteriorated markedly on the background of a pessimistic macroeconomic outlook. Besides, uncertainty in financial markets, which adds to an already fragile banking sector, is having a very negative impact on the conditions for company investment.

Uncertainty is at its highest since the recovery started, and a sense of urgency is missing given the current context. We cannot afford to be pure spectators of economic and financial developments only to act late, with weak and uncoordinated decisions. We need to be on the driving seat.

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In recent months it has appeared that policy decisions have been responding to the course of economic and financial developments. In acting early and in a co-ordinated, consistent and decisive way, policy makers can break this vicious circle and restore confidence.

In order to ensure macro-financial stability, and safeguarding the Euro, requires strong action at both the EU and national level.

Firstly, improving economic governance, and secondly, restoring fiscal sustainability through a smart consolidation of public finances and implementation of growth-enhancing structural reforms.

These two overarching objectives are equally necessary and mutually reinforcing, so that they will only work if both of them are implemented vigorously.

1. At EU level

Safeguarding the Euro is an absolute must. Company investment depends on it. There is no other option than to secure the stability and credibility of our common currency.

We have moved one step forward with the vote from the European Parliament on the 6-pack last week. This has meant compromises on all sides. But it has shown that all parties recognized that building confidence in Europe's economic governance is essential in order to create the conditions for long-term growth. We must now to focus on implementation, ensuring that rules are fully respected.

We also welcome the euro-group agreement made on 21st July. It put forward a comprehensive package for Greece and improved financing terms for Portugal and Ireland. The measures to increase the powers of the EFSF (European Financial Stability Facility) and its successor the ESM (European Stability Mechanism) were particularly important. We have called on Member States to take swift and decisive action to quickly ratify the 21st agreement in a manner that increase market confidence.

Looking ahead, taking into consideration the continuing financial market uncertainty, it is clear that more radical reform may be required to safeguard the euro.

Whatever decision comes next, it is important that a clear and complete strategy is underlined. Partial reforms that focus only on austerity will not work. Growth-enhancing reforms must come along with it. In the same way, we cannot pursue a strategy that ignores the link between banking and sovereignty crisis. However, any realistic proposal regarding new financial instruments needs to ensure that proper incentives are put in place for Member States to improve fiscal discipline.

2. At Member State level

At national level, it is important that Member States take decisive actions to both improve the long term sustainability of their public finances, and implement growth enhancing economic reforms, to increase its long-term potential.

We believe that fiscal consolidation can best contribute to raising growth if measures are focused primarily on reducing and improving the efficiency of public spending, rather than increasing taxation.

This implies not only reducing public indebtedness, but doing so in a smart way, rationalizing and re-shifting spending priorities towards productive uses.

This means combining an exit strategy to cap public indebtedness with an entry strategy, investing in innovation, skills, technology and modern infrastructure.

Here the focus of reforms should lie on improving the quality of public expenditure, while at the same time enhancing competitiveness in the EU.

The financial and economic crises do not explain the difficulties that European economy faces. The impact of the crisis has been very uneven, with large country divergences when it comes to growth and employment. In fact it is clear that those countries which maintained a sustainable competitive position well in advance of the crisis, such as Germany, are generally those that have been most resilient during the crisis.

By the contrary, for countries having accumulated large debt and competitiveness imbalances before the crisis, this implies important challenges.

An internal rebalancing requires an ambitious policy response, not only at the fiscal level, but also by addressing labour and product market rigidities, and by improving adjustment mechanisms.

The crisis has clearly demonstrated to us that competitive adjustment channels are not functioning properly or quickly enough. This is particularly true in the euro area.

Regarding labour market reforms, in our latest publication, “Putting Europe to Work”, we have issued 14 specific recommendations to improve the functioning of labour markets.

Let me touch upon the most relevant:

- Wage setting is not a European competence. That being said, it is in the common interest of social partners at national level to improve wage flexibility
- If not, employment will be the main variable of adjustment. Automatic indexation mechanisms that act as inflation transmission belts are counterproductive.
- Increase adaptability and skills of the labour force, while adopting labour market reforms towards “flexicurity” principles in order to facilitate job creation.

Structural reforms should also be targeted at improving competition and addressing rigidities in product and service markets, providing opportunities for entrepreneurship and tapping the potential for investment and job creation
Finally, a balanced agenda for the financial sector reform is also essential. In this context, effective financial supervision is crucial to ensure confidence in financial markets and improve financial stability management.

Financial reform measures should be aimed at improving access to capital for companies and increasing market liquidity while at the same time preserving market integration.

Regulation should based on comprehensive impact assessments that take into account the global nature of financial markets and the cumulative effect of financial reform measures.

To conclude, as the IMF has highlighted, the EU economy has entered a very dangerous phase, which requires policy makers to take bold action.

Restoring confidence will depend on the strength, thoroughness, and timeliness of the policy response to the exceptional uncertainty that we are surrounded with.

Increasing long-term growth and ensuring fiscal sustainability can only be done by undertaking the types of far reaching reforms I have described.

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