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SHORT-TERM ECONOMIC PROSPECTS AT INTERNATIONAL LEVEL
AND FOR THE COMMUNITY

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At the last European Council meeting, held in The Hague in June 1986, participants were somewhat perplexed by the contrasting pattern of economic developments. On the positive side, firms and consumers had become more confident and purchasing power and incomes in the industrialized countries had risen following the sharp fall in the dollar and in oil prices. On the negative side, world trade had contracted between the autumn of 1985 and the spring of 1986 while the pace of domestic economic activity in the Community's large countries had remained modest in some cases and mediocre in others. Two main explanations were put forward:

- faced with rapid and far-reaching changes in their environment (energy prices, fluctuations in the dollar), firms and consumers, especially in Europe, had adopted a wait-and-see attitude,
- the persistent imbalances in international monetary and financial relationships were preventing a return to rapid growth in world trade.

What is the situation today?

According to the studies conducted by the leading economic research institutes, growth prospects at the end of 1986 are slightly worse than the forecasts made a year ago, notably in the case of the Community.

First, the world economic environment as it affects the Community is characterized by what could be termed semi-controlled disorder.

The main recessionary risks appear to be receding in the short term. However, the situation in the United States must be watched with the utmost vigilance. Together with the debt crisis, this is probably the main source of uncertainty.

For one thing, the sharp plunge in oil prices brought with it the danger that a large number of oil-producing countries might suddenly end up insolvent. For the moment, mainly because of the upturn in world oil demand (some 2% a year), a compromise situation has been restored within OPEC. After falling to US \$ 10 a barrel, the price of crude oil is expected to stabilize at between US \$ 12 and US \$ 15 next year, depending on the degree of cohesion within OPEC. However, there would seem to be no prospect of sufficient discipline being exercised to bring the price back to around US \$ 20 a barrel.

Second, there is hope that the deterioration in the terms of trade since 1983 of the countries producing raw materials other than oil will be arrested. The volume of imports by the developing countries, with the exception of those in Africa and the OPEC countries will probably show a small increase next year of around 3%.

Turning to the world's dominant economy, that of the United States, whose performance exerts a strong influence on the world economic trend, both qualitatively and quantitatively, we should remember that views of the situation differ widely between Europeans and Americans.

In the Europeans' opinion a further fall in the dollar against the ECU and the yen, even a very sharp one, would not rapidly eliminate the US trade deficit, no more than would a reduction in interest rates in Europe. The point must also be made that faster growth in Europe would have only a very small impact on US exports. This is because 60% of US exports go to, and 55% of imports come from, countries whose currencies move in line with the dollar. If we also bear in mind that US fiscal policy will remain accommodating next year (with a deficit approaching US \$ 190 000 million), the conclusion cannot be avoided that the performance of America's domestic economy is not very encouraging in the short term, especially as the structural weaknesses of part of the productive potential are now more clearly visible.

Economic growth in Japan has slowed down and the country is continuing to do little to help sustain world demand. What is more worrying for us Europeans, its industries are continuing their forceful marketing drive in Europe in a bid to offset the decline in their exports to the United States.

Overall, the expected growth of world trade is seen to be insufficient to help resolve the problems facing both the developing countries and the debt-burdened countries.

For the growth of world trade to show a permanent improvement, further progress must be made in international cooperation on the monetary, financial and trade fronts.

Recognition of this need would be a renewed source of hope for us all. But such progress is very difficult to secure as two recent events show:

- Even though there may be doubts about how far the US/Japan monetary agreement can be carried through in practice, it does reveal an attempt to establish a hegemony based on an understanding between the two powers on either side of the Pacific;

- In Lima, on 15 November, thirty-five of the most heavily indebted countries repeated their doubts about an orderly settlement of the debt problem on a multilateral basis with the IMF and the World Bank as the main actors.

These two examples remind us just how urgent it is for Europe to speak, propose and act with a single voice. It did so successfully at Punta del Este, where a new round of trade talks was launched. It also showed it was capable of doing so at the meeting of Economic and Finance Ministers at Gleneagles when faced with the possibility of a sharp drop in the dollar. It will have to continue to do so in the fields of monetary cooperation, aid for developing countries and the search for stronger, more employment-intensive growth. What are the prospects for such growth?

Most Community countries are currently experiencing a recovery fuelled by private consumption, which is helping to sustain the previous expansion in investment.

In those countries where external performance picked up fastest, this development is reinforcing the existing growth of investment.

In the countries where the external adjustment is more recent, the expansion in investment will probably accelerate next year.

In all, economic growth in the Community in 1987 is expected to be in the region of 2.5-3%, slightly up on 1986 (around 2.5%).

However, it would appear that this momentum has now reached its maximum strength. The growth rate will probably decline again to between 2% and 2.5% during the second half of 1987, for two reasons: a number of countries have already taken very stringent measures in 1986 to curb activity, notably with a view to rectifying persistent

imbalances in public finances; more generally, however, the stimulus provided to private incomes and consumption by falling energy and commodity prices will gradually diminish while the prospects for export volumes will remain very poor.

Thus, at the time when the improvement in the external terms of trade is producing its maximum effect, growth in the Community will next year permit only a very slight reduction in unemployment.

This could not be tolerated. Hence the guidelines issued by the European Council in The Hague concerning practical implementation of the cooperative growth strategy and steps to improve the operation of the labour market and encourage the setting up and expansion of small and medium-sized businesses. As requested by the current Presidency of the Council, these two matters are dealt with in a separate document.

The cooperative growth strategy, the details of which have been updated by the Commission's latest annual economic report, has the support of both the employers' organizations and the trade union organizations in the Community, which adopted a joint statement on 6 November (see annex).

The strategy is based not on the so-called locomotive theory, but on the contribution that all Member States can make to growth in the Community, with some exploiting the room for manoeuvre secured through their excellent performances in restoring domestic stability and earning external surpluses, and with others continuing their adjustment policies while, at the same time, all of them encourage the investment that is absolutely essential to any improvement in the quality and size of productive potential in the Community.

JOINT OPINION ON THE
COOPERATIVE GROWTH STRATEGY FOR MORE EMPLOYMENT

An in-depth exchange of views on the economic situation and employment in the Community was held at the meetings of the Macroeconomics Working Group (set up after the meeting between UNICE, CEEP and ETUC with the Commission on 12 November 1985), and the Commission's Annual Economic Report 1986-87 was discussed.

UNICE, CEEP and ETUC confirm their agreement on the basic principles of the Community's "Cooperative growth strategy for more employment" and support the general thrust of the economic policy proposed by the Commission in its Annual Economic Report 1986-87.

They call on the Governments of the Member States to make a greater effort to ensure that the cooperative strategy is effectively implemented and declare their willingness to cooperate.

Full or broad agreement was reached on the following points:

1. In spite of the progress made on the employment front, unemployment is still too high. Unless additional efforts are made, it will not fall sufficiently in the medium term. The aim in implementing the cooperative growth strategy is to bring about a significant and lasting reduction in unemployment over a period of several years. In order to do this, more jobs must be created through increased investment based on improved business profitability and reinforcing the competitiveness of the European economy. Public investment also has an important role to play in this respect, without jeopardizing the medium-term consolidation of public finance.
2. The creation of durable jobs will be threatened if inflation rates are not kept low. A stable financial environment encourages the propensity to invest. Monetary and budgetary policies should be managed in such a way as to ensure that inflation rates remain low or continue to fall. The social partners also share some responsibility for containing inflation.
3. Real interest rates should fall further, with account being taken of the world economic situation and savings behaviour. The liberalization of capital movements should help direct savings towards productive investment.

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4. The internal market must be completed rapidly. This will make it possible to release considerable growth potential which will reinforce the positive effects which the implementation of the cooperative strategy will have on investment and growth. Completion of the internal market should be accompanied by taking account of social policy and by the development of structural policies to strengthen the Community's economic and social cohesion as it is defined in the Single European Act.
5. Research and development must be promoted so that the Community maintains or regains its technological competitiveness, particularly in high-tech sectors. The Community should also encourage the implementation of the major "mobilising programmes" which are such as to promote growth and employment.
6. Improving the level of skills in the labour force and vocational retraining are important elements in developing employment and the competitiveness of the European economy. Training costs represent an investment. Employees at every level should be encouraged to take training courses.
7. The freedom of world trade should be maintained and developed within the framework of GATT. The Community has a special responsibility in this respect. Generally, an effort must be made to continue to combat protectionist trends, unfair practices and escalating subsidies, the effect of which is to distort the conditions of competition. In certain cases, temporary bilateral or multilateral agreements could help to overcome specific problems.
8. In the framework of the cooperative strategy, moderate growth of real per capita wage costs below productivity gains should be maintained for some time to come in the countries in which it is already practised, and it should be applied in the other countries. But the other elements of the strategy must be implemented simultaneously. This will make an important contribution to improving business profitability and competitiveness as well as speeding up the implementation of job-creating investment. It is important here to highlight the link that exists between the moderation of wage costs - factor for increased profitability - and higher employment.
9. Appropriate tax measures, the development of new forms of financing, and easier access to risk capital can also strengthen investment and employment, notably in small and medium-sized firms.
10. Public investment and infrastructure investment have suffered under the process of budgetary consolidation, and there is at present some leeway to be made up here. Stronger expansion of such investment will make

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an important contribution, on both the supply and the demand sides, to achieving higher and sustained growth. Such investment should be regarded not as a way of compensating for the lack of private investment, but as complementary investment undertaken in the general interest. Its financing could be achieved in the framework of a healthy budgetary policy through the restructuring of budgets and through the use of budgetary headroom that already exists or will be created by the growth process; furthermore, in a number of major instances, reliance on private financing seems possible and desirable. In this connection, the following distinctions were made:

- a.) public investment or infrastructure investment which is profitable in itself but which, without public initiatives, would not be carried out at the appropriate time because of its scale or because of its long pay-off period (for example, the Channel tunnel and the high-speed-train link between Paris, Brussels and Cologne); in the case of this type of investment, private financing can most easily be envisaged;
- b.) public investment or infrastructure investment which is economically profitable in overall terms because it represents a precondition for private investment or for the development of certain countries or regions; in the case of this type of investment, on the basis of rigorous economic calculation, certain forms of cofinancing by the private sector can be examined;
- c.) public investment intended to meet justified public or social needs; its profitability must not be seen solely in economic terms; deciding on the priority projects in this area is also a matter of political judgement; cofinancing by the private sector is more difficult to envisage, but not to be ruled out in all cases.

UNICE, CEEP and ETUC are convinced that dialogue is an important element in the effective implementation of the Community's cooperative growth strategy for more employment. They are prepared to continue the dialogue, especially on questions not yet resolved (e.g. reduction in government spending and in taxes and social security contributions, the adaptability of financial, commercial and labour markets, revision of certain regulations, more flexible wage formation, reorganisation and duration of working time, etc.).