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MIXED ECONOMIC TRENDS FORECAST FOR 1985 BY E.C. COMMISSION

A gradual economic recovery is under way in the European Community, but unemployment remains a "dominant problem" reflecting structural flaws in the economy, the Community's 1984-85 annual economic report concludes.

The Community's economy is expected to grow by 2.2 percent in 1984 and 2.3 percent in 1985, an improvement over its performance in recent years. The news on inflation is good, with prices expected to rise only 5 percent in 1984 — compared with 11 percent in 1980.

At the same time, however, the average annual unemployment rate in the Community is expected to be 11 percent in 1984, and rise to 11.5 percent in 1985. That compares with 10.4 percent in 1983, 9.5 percent in 1982 -- and only 6.1 percent in 1981.

The report, which was prepared by the E.C. Commission, recommends a variety of measures aimed at expanding the Community's economy and creating jobs, including lower taxes, less regulation of business and reduced labor costs.

The report notes that the Community has taken positive steps this year to solve its budget problems and promote information technology, creating a momentum that could be carried forward to the employment situation. With a new European Parliament elected in June and a new Commission taking office in 1985, "conditions are now particularly appropriate for intensifying a collective effort to turn employment trends in a far more positive direction," it says.

Unemployment problems have been particularly acute among young people and women, and long-term unemployment has increased substantially, the report says. Of the E.C.'s 10 member states, only Denmark, Italy and the United Kingdom are expected to show employment increases from 1983 to 1985. Millions of jobs have been created in recent years in the services sector, partially offsetting losses in industry. But many of them have been in the public sector -- a trend that cannot be sustained under present budgetary constraints, the report says.

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Among the report's recommendations are these:

Capital vs. Labor. The Community must correct its bias toward "capital deepening," i.e., capital that replaces labor rather than expanding the overall economy. In contrast to the United States, where both industrial investment and employment have risen, increased investment in the Community has not created new jobs. An important factor in this trend is undoubtedly the persistent rise in real labor costs in relation to the rate of return on investment. The Community's economic growth must be channeled more in favor of employment, which does not mean neglecting technological progress or reducing investment -- as demonstrated by the strong technological performance of Japan and the United States, which do not share the Community's labor-saving bias.

Taxes. The Community should lighten tax burdens that discourage businesses from expanding production and creating jobs. These burdens include rising social-security charges on employers and income and social-security taxes on employees that increase pressure in wage negotiations for higher pre-tax salaries. The Community should consider reducing the tax burden's share of the Gross Domestic Product by one percentage point a year from 1985 to 1987. Its share of G.D.P. this year is 42.4 percent.

Regulation. The Community's member states should review the mass of regulatory requirements, especially those affecting creation of new businesses. France, for example, recently streamlined statutory formalities for launching new enterprises, introducing a one-month maximum administrative delay. The United Kingdom has taken steps to increase competition in the financial, legal and medical professions, which have been unduly restricted. It has also embarked on a large program of privatization and deregulation in the telecommunications, air and road transport and petroleum sectors, and in several manufacturing industries. France, the Federal Republic of Germany and the United Kingdom have prepared tax changes favoring the start-up of new, small businesses.

Regulation of the labor market by legislation and collective-bargaining agreements should also be relaxed. Problems include rules that prevent fixed-term contracts, impose heavy conditions on layoffs, restrict or impose disproportionate costs on part-time work, and require minimum wages in certain job categories that discriminate against young people seeking their first jobs.

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Labor Costs. Increases in real wages should be strictly controlled, and perhaps tied partly to profits or performance. Combined with reductions in employment taxes and the costs associated with undue labor market regulation, wage moderation would create a situation more favorable to employment.

Public Spending. The Community should maintain the recent check to the rise in government spending. As a share of Gross Domestic Product, public expenditures in the Community fell in 1984 for the first time in the postwar period. After reaching a peak of 47.8 percent of G.D.P. in 1983, they dropped to an estimated 47.3 percent in 1984.

The Community should consider as a medium-term objective trying to reduce government spending as a share of G.D.P. by one percentage point a year.

Industrial Technologies. The Community has launched an effort to compete with Japan and the United States in the area of technological innovation. In addition, the education system must be adapted to producing technical and managerial skills. The tax system and capital market institutions must provide a financial environment favorable to innovation and risk-taking investment. The Community's competition policy should favor collaborative research and development efforts of European businesses.

Training. Vocational training and employment should be offered to young people to build up the availability of technical skills.

World Economy. The Community should develop cooperative action with the United States and Japan to obtain a better balance of their economic performances, particularly when the U.S. takes action, as expected in 1985, to correct its budget deficits. The E.C. should also continue to support trade liberalization programs and development aid that eases the debt problems faced by developing countries.

The "Annual Economic Report 1984-85" also includes economic reviews for each of the 10 E.C. member states. A separate Commission report, "Annual Economic Review 1984-85," contains detailed information about the Community's labor market, business and household sectors, and budgetary and monetary policies. Both reports will be published shortly as issue No. 22 of the Community publication European Economy. They will be available from the European Community Information Service, 2100 M Street, N.W., Suite 707, Washington D.C. 20037. The price is $7.