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THE ECONOMIC AND SOCIAL SITUATION IN THE COMMUNITY

(Working paper of the Commission to the European Council
29 and 30 March 1985)

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Working paper presented to the European Council

1. Introduction

At its last meeting in Dublin, the European Council underlined the priority given to the problem of unemployment. It considered that the guidelines embodied in the most recent Annual Economic Report should be speedily implemented and asked the Council to take appropriate action.

The European Council asked the Council and the Commission "to report back to its meeting in March on what measures might be appropriate for the Community or may already have been initiated to assure the objective of a progressive increase in the actual and potential growth rate for the Community to the benefit of employment".

Such is the object of this working paper.

2. Trends and prospects

There is at present no evidence that the European or world economic recovery is faltering.

2.1 In the Community inflation rates are falling and becoming more convergent. The current balance of payments situation has improved. GDP is expected to grow by 2.4% in 1984 and 1985. This figure is slightly higher than that assumed in the last annual economic report.

There has been no radical improvement in the employment situation. While 1985 is likely to see a slight increase in employment over the Community as a whole, unemployment is still at a high level and may even be somewhat higher in 1985 (11.2%) than in 1984 (10.9%). The labour market situation therefore remains highly unsatisfactory. With a continuation of recent trends, and without further measures, it is unlikely to become any more acceptable over the next few years.

2.2 At the world level economic recovery is also continuing. The slowdown in growth in the United States is currently proceeding relatively smoothly (1984: 6.8%; forecast for 1985: 3.5%), although budget policy corrections have not yet been made and leading indicators do not provide a clear picture. From the viewpoint of the European economy, the erratic movements and upward trend of the dollar exchange rate provide cause for concern in the short term, since they could lead to an undesirable rise in European interest rates. The dangers inherent in the continuing and increasing budget and balance of payments deficits have in no way diminished. The higher the dollar rises and

the longer the delay before deficits are cut, the greater could be the eventual adjustment problems. This provides serious cause for concern as to the growth of the world economy and international trade and as to the operation of exchange and capital markets.

3. Recent economic policy developments

Since the Community's economic strategy, as adopted by the Council of Ministers in the last annual economic report, is essentially a medium-term strategy, it is not surprising that there have been no major changes in economic policy in recent months. Monetary policy, underpinned by the EMS exchange-rate mechanism, continues to aim for stability, although the anticipated rise in dollar interest rates has interrupted the downward trend in short term rates in Europe. If the dollar continues to appreciate, there may be undesirable repercussions for domestic economies in the form of higher interest rates, as has already happened in the United Kingdom.

Budgetary policy remains one of consolidation, although in some countries budget deficits in 1984 turned out to be somewhat larger than hoped for.

The moderate rise in nominal and real wage costs is likely to continue in most Community countries in 1985.

4. Is there any room for an economic policy that would be more beneficial to employment?

The Commission did not propose any adjustment in the economic policy guidelines to the Council of Ministers. This does not mean that it is satisfied with the results achieved.

The task now is to implement the economic strategy rapidly, to develop it further and to emphasize certain features. Further progress must be made on the prices and balance of payments fronts in a number of countries. For the Community as a whole, however, employment has first priority. There is therefore a continued need to achieve higher growth than the forecast rate of just under 2.5% on a healthy and sustainable basis, and in particular to bring about more employment-intensive growth with a higher rate of job creation for each percentage point of growth.

The conditions for this have improved:

- the smooth functioning of the EMS exchange-rate mechanism has led to a very distinct improvement in the convergence of policies and in the results achieved, notably in terms of inflation and balances of payments;
- moderate wage settlements have improved business profits and strengthened the propensity to invest in many Community countries, even though too many firms still hesitate to make use of their capacity for self-financing because of the weakness of demand;
- the two sides of industry, both employers and unions, seem more open to dialogue. This is at any rate the impression the Commission has gained from the dialogue which it has sought to revive with and between them;

- the awareness has grown among those responsible for economic policy that no Community country can alone solve the problems of employment and employment-intensive growth and at the same time safeguard stability. No Member State can secure a sustainable increase in growth simply by stepping up its exports to other Member States. It should be remembered that 50% of Member States' foreign trade is carried on between them. This underscores the degree of interdependence that exists but also the limits to any plan for underpinning growth in one country by boosting demand in the others. Each country must therefore focus more closely on bolstering its own domestic demand? This therefore is a Community-wide problem.

Use must be made of the economic and political room for manoeuvre created in this way.

- (i) Implementation of the Community's economic strategy will be all the more effective the broader the consensus on which it is based.

Hence the importance of the industrial dialogue between the two sides of industry and of negotiations at all levels (e.g. at company level, at industry level, at national level and at Community level). The fields in which progress would seem possible include the introduction of new technologies, the functioning of labour markets as it affects the distribution of work, and even macroeconomic matters such as reconciling moves to bring costs under control with moves to underpin demand;

- (ii) There is broad agreement between Member States' governments on the need further to improve supply conditions in the economy. Since the policies followed are slow in acting, this may hamper their social acceptance. On the other hand, if economic activity were more buoyant, it would be easier to improve supply conditions. Steps should be taken to add a dynamic element to the necessary policy mix of budgetary consolidation, monetary stability and wage cost moderation. This could be done by aiming for stronger growth in public and private investment. The countries in which the process of consolidating public budgets has already made sufficient headway should make full use of the existing and future room for budgetary manoeuvre as a means of fostering investment. This would be a contribution to economic dynamism and positive adjustment that would be not only in the interests of each individual country but also in the common interest. The Community can itself play a part in the process. For this purpose, consideration could be given to a further development of its borrowing and lending instruments, especially as part of a programme of investment in transport and telecommunications infrastructures commensurate with a large economic area in which internal frontiers have been dismantled. This would contribute to attainment of the key objective of creating a vast internal market.

5. To sum up, the Commission proposes to the European Council that:
- it should reaffirm the objective of an appreciable reduction in unemployment within a reasonable period, to be achieved with the help of higher and, in particular, more employment-intensive growth that does not jeopardize monetary stability;
 - implementation of the Community's economic policy strategy should be helped by reactivating the industrial dialogue at all levels; as part of the dialogue and, where appropriate, with the Commission's support, employers and unions should draw up, in time for the European Council meeting in December 1985, proposals on how they can contribute to attainment of the joint objectives;
 - the Member States and the Commission should examine how each country can ensure that control of expenditure and budget deficits is more closely reconciled with economic dynamism; expenditure that helps to underpin activity and to prepare for the future should be identified, together with the reductions in taxation that would do most to boost investment and create jobs;
 - the European Council should lend its support to the Commission's intention of examining the extent to which the Community could itself, through its borrowing and lending operations, assist and foster this overall strategy.