SPEECH

PUBLIC HEARING ON THE SPREAD OF THE CRISIS

14 JANUARY 2010, EUROPEAN PARLIAMENT - BRUSSELS

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Ladies and Gentlemen,

It is a great pleasure and honour to be here and share with you some lessons that we, in the business community, have drawn from this crisis and its impact on the economy.

But let me start by saying few words of the causes. These are well known by now:

- Monetary or exchange policies which flooded financial markets with excess liquidity;
- The attempt to achieve high yields on this liquidity without an accurate assessment of risks by markets or regulators;
- Excessive leverage;
- An absence of regulation or inappropriate regulation of certain financial activities;
- Inadequate coordination of economic policies and insufficient reforms (particularly in the EU);

These are real dysfunctions which have had serious consequences for our economies and labour markets. But the worse has been avoided.

First lesson: decisive interventions by central banks and governments were needed and have paid off. The recession was deep but relatively short-lived.

After five consecutive quarters of contraction, a fragile recovery is currently under way and growth in the EU should reach around 1% this year.

This is a fragile momentum. Neither self-sustained nor sufficient to restore job creation. But it is there and it proves the success of stabilisation policies.

In Europe, a key moment was the emergency summit of euro-area Heads of States with Prime Minister Brown, President Trichet and President Barroso on 12 October 2008.

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The bank rescue plan that was collectively agreed there was a critical step to restore confidence, at a moment when the global financial system was on the verge of collapse[1].

This being said, implementation of this plan was uneven and the individual measures taken by Member States have created significant distortions to the internal market.

This exposed important weaknesses in the EU and global crisis management toolkit. Procedures to respond to cross-border failures and to ensure adequate and swift burden-sharing were simply not in place.

From the start of the crisis, we underlined that cross-border supervision was deficient and had to be reinforced urgently. BUSINESSEUROPE was an early supporter of the reforms proposed by the de Larosière group.

The compromise reached last December in the Council to set up the new EU supervisory bodies is not flawless but it is a suitable compromise that provides a good basis for discussion with the European Parliament.

A necessary complement to the proposals is to set clear criteria for early cross-border interventions, common burden-sharing and improve resolution regimes for cross-border financial institutions.

Financial market integration must remain a core objective. Segmenting the internal market for financial services would have great consequences for the functioning and competitiveness of the European economy and its companies.

Second lesson: the banking crisis is contained but credit constraints for companies will intensify

Bank lending flows to companies have turned negative in recent months and lending standards continue to be tight, in particular for SMEs.

Companies have responded to the credit crisis by slashing their investments and by deleveraging their balance sheets. But the demand for credit is still there. This is clearly illustrated by the record volume of issuance on corporate bond markets during 2009.

We fear that financing constraints will increase when activity picks up again. Banks are still in a weak position and will not be able to expand significantly the amount of credit to support the recovery. This could be an important stumbling block for the recovery in Europe, where 2/3 of companies external financing are channelled through bank loans.

So, yes, we are very concerned about access to credit for companies. This upturn will not go anywhere without a sufficient level of financing. What should be done?

[In March last year, our organisation issued 16 recommendations to facilitate access to finance for companies (Betbeze report). These were mostly emergency measures. We are quite happy to see that most of these were implemented, in particular by the ECB

[1] the plan involved state guarantees to unfreeze money markets, commitments to re-capitalise financial institutions and exceptional liquidity interventions by the ECB

and the EIB. The focus should shift now towards exit strategies, reforms and new channels of financing.]

We expect the ECB to show the same control and leadership to sustain a fragile recovery as it did in responding to the crisis. Given the impeccable track record so far, I have little doubt that Mr Trichet and his team will succeed in developing the right policies;

The consolidation of banks' balance sheets must be pursued with urgency and exit strategies from state interventions in the financial sector must be well timed and coordinated to avoid risks of further instability;

Financial market reforms should temper past excesses but not constrain the availability of finance for future investments. There is a difference between ambitious reforms and rushed decisions. This is particularly true when deciding on new capital rules for banks. Proposals so far are piecemeal and lack a comprehensive assessment of their impact on growth and job creation;

Broader access of SMEs to financial markets and ways of reinforcing equity finance and venture capital will need to be developed. This will be an important issue for in coming months.

Third lesson, the shift from private to public debt is unsustainable

The average public debt to GDP ratio in the EU will reach 80% this year and 100% by 2015 under a no-policy-change scenario.

This is not some long-term concern that we can tackle at a later stage. It is an issue for the strength of the recovery in the next few years.

If governments are unable to restore confidence in public finances, punishment will come rapidly from markets, companies and consumers: long-term interest rates will rise and investments will be cut.

Restoring confidence in public finances requires clear commitments on "when" and "how" to consolidate. Exit strategies must be planned at the latest in 2010 and fiscal consolidation should start in 2011. The Stability and Growth Pact remains the appropriate instrument to coordinate the necessary return to fiscal discipline.

But the nature of consolidation measures is as important as credible deficit targets. Higher taxation, particularly on labour and capital, will do lasting damage to growth and job prospects.

The priority must be to reduce public spending and rebuild the tax base through growth-enhancing reforms. This implies new thinking on the effectiveness of public administration, public investment, social systems and tax structures.

Greater focus on debt sustainability and structural reforms will be key to combine growth and fiscal consolidation in the years ahead.

Consolidation strategies will be an integral part of the EU's growth agenda for the next 5 years.

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Fourth lesson: tackling labour market challenges will require structural reforms

European companies, helped by governments and a constructive attitude of workers and their representatives, have made great efforts to limit job losses.

The deterioration in labour market conditions has so far been more muted than initially expected in most countries. But it has been significant, particularly in a handful of countries (Spain, Ireland and Baltic States). The unemployment rate is now reaching 9.5% in the EU and 10% in the euro area.

Short-time working arrangements have been quite useful in some cases. But they are temporary.

So we need to put in place measures and policies that will help to address the social and employment impact of the crisis while increasing the efficiency of our labour markets in the long run.

Structural reforms aimed at stimulating labour demand and reducing benefit dependency will allow labour markets to recover more quickly.

Crucially, they prevent rising unemployment from becoming entrenched. This is particularly relevant for the EU which has historically been struggling with high levels of structural employment.

The key word for the recovery will be “adaptability”: Adaptability of our labour markets to take advantage of globalisation and new structural shifts; Adaptability of our companies to remain competitive and innovative; But also adaptability of workers to a fast-changing environment. That is why the implementation of flexicurity is so important. It facilitates the creation of new jobs, supports people during transitions, and develops skills through training.

Policy-makers will have to come up with measures that strike the right balance between immediate needs resulting from the crisis and long-term policy challenges. The adaptability of our companies and workers will be key.

Fifth lesson: Europe is lagging behind in the global upturn. It needs to catch up.

Since April 2009, international trade volumes have picked up by 8.5% but EU exports have only increased by 2.5%. Industrial production in emerging Asia has increased by 7.5%. In Europe, it has only stabilised and is still down by more than 13% on a year earlier.

Europe must reinforce its capacity to compete on global markets and increase its growth potential back to at least 2% (from 1% at present).

This is not a normative objective but a necessary condition to sustain our social model and our way of life in the future.

A common and ambitious EU growth strategy must be put in place. We are happy that President Van Rompuy has convened a special summit to discuss this issue in February.

EU institutions and Member States must feel collectively responsible for the success of this strategy and be held accountable for their contributions in coming years.

A new impetus for EU's internal market, greater emphasis on knowledge and skills and a truly integrated industrial policy will be particularly important.

The whole credibility of the strategy will rely on the ability to set realistic and measurable objectives to be achieved over the next five years by the Commission, the European Parliament and the Council.

With the entry of the Lisbon Treaty into force, we believe that a stronger and more effective system of economic governance can be put in place in Europe. This is an opportunity that EU institutions should not allow to pass by.

Sixth lesson: global economic governance must be improved

G20 leaders concurred that global imbalances were a major factor in the crisis.They called again in Pittsburgh to reinforce cooperation and coordination of economic policies.

But we are a long distance away from this objective. The defensive position of China on its exchange rate policy and benign neglect of US authorities for the external value of the dollar are an illustration.

We are concerned about this, not only for European exporters but for global financial stability.

The perpetuation of very loose monetary policy in the US, a weak dollar and the peg of Asian currencies could recreate the conditions for asset price bubbles. Some indications of that can already be seen in recent financial markets and in commodity prices.

Let me conclude

Exceptional measures have successfully stabilised our economies. A tentative recovery is currently under way. But public interventions in the economy have reached their limits and Europe is lagging behind in the global upturn. To sustain growth, support job creation and restore the viability of public finances, Europe must embrace change and implement far-reaching reforms.

Global economic governance will also need to be considerably reinforced to avoid repeating past mistakes.

This is hopefully a message that will come through during the Informal EU Summit on 11 February which should create real sense of urgency and develop a ambitious growth strategy for Europe.

Thank you for your attention....