



Business and Industry Advisory Committee to the **OECD**

Comité Consultatif Economique et Industriel Auprès de l' **OCDE**

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## **BIAC Statement to the EVIAN G8 Economic Summit**

**Paris, 19 May 2003**

### **A Market Economy in Times of Prevalence of Risk**

BIAC is pleased to submit this statement to the Evian G8 Summit on behalf of the business communities of the OECD's member countries. **We are firmly of the opinion that the deliberations of the G 8 should be squarely based upon the analytical work of the OECD and supported by its fact-based policy formulae.**

The prevalence of risk in the world economy and how to enhance growth stay high on the business community's agenda. The enhancement of structural policies to create growth as well as the continued reduction of trade and investment barriers remain core business messages that we would like to deliver to the Evian G8 Summit. Our summary view of the economic situation indicates a differentiated picture, supporting the results of numerous OECD studies that growth trends have diverged through the 1990s and into this decade:

- **The global economy is on a 2.0% GDP expansion track improving to 2.9% in 2004.**
- **Less geopolitical uncertainty can lead to stronger consumer confidence with improving business sentiment and capital investment to follow.**
- **In the first Quarter of 2003 the U.S. economy grew 2.1%, with robust IT investment, up 6.7%.**
- **Europe's growth is constrained by a lack of economic reforms, and a soaring euro.**
- **Japan is in another round of slow economic recovery, but resilience remains uncertain.**
- **Canada's growth beats the U.S. pace due to employment and consumer spending gains.**
- **SARS will limit near-term activity in some Asian-Pacific countries, but rebounds should be swift.**

### ***Reboost for globalisation needed***

The global economy is in the midst of a phase of weakness. The global mood is decidedly gloomy. In nearly all industrial countries, but also in the newly industrialising economies and the countries of Central and Eastern Europe, growth of real Gross Domestic Product (GDP) has slowed again during the winter half year. In the United States this basic underlying trend was eclipsed by the spending on the Iraq War.

In line with the escalation of the Iraq conflict and, related to it, the increasing world-wide uncertainty regarding economic and geopolitical developments, economic recovery has stalled once again. This economic weakness stems from numerous factors such as war, threats of war, terrorism, corporate scandals, sinking equity markets, the complexities of the current business cycle, the depressed investment confidence of both businesses and consumers.

In an economic sense this is doubly unfortunate, for globalisation has opened borders to ideas, investment and capital flows, and the movement of people and production according to basic market incentives. People and cultures have interacted in new and expanding ways. Importantly, societal and cultural forces are melding, reinforced by commercial ties.

Market-based economies facilitate globalisation because of the quest for greater economies of scale and associated efficiencies, lower costs, scarce skills, higher productivity and ultimately profit and other returns to entrepreneurship. In fact, globalisation transmits both good and bad pulses at rapid speed. At the moment we are watching synchronous global economic stagnation exacerbated by geopolitical events which develop as fast as others are contained or resolved.

***An outlook...***

Global economic expansion is stubbornly slow, at a 2.0% pace, even as geopolitical uncertainty abates. This is not much better than last year's expansion but **cumulative** growth should be sufficient to boost capital equipment investment 2.6% this year after last year's 1.2% decline.

**Real GDP Growth Rate Comparisons  
(Annual Percent Change)**

	<b>Actual</b>		<b>Current Outlook</b>			<b>November 2002 Outlook</b>	
	<b>2001</b>	<b>2002</b>	<b>2003</b>	<b>2004</b>	<b>2005</b>	<b>2003</b>	<b>2004</b>
<b>World</b>	<b>1.2</b>	<b>1.9</b>	<b>2.0</b>	<b>2.9</b>	<b>3.1</b>	<b>2.6</b>	<b>3.0</b>
<b>Americas</b>	<b>0.3</b>	<b>2.0</b>	<b>2.1</b>	<b>3.2</b>	<b>3.5</b>	<b>2.8</b>	<b>3.3</b>
U.S.	0.3	2.5	2.2	3.2	3.5	3.0	3.3
Canada	1.5	3.4	2.7	3.2	3.4	3.2	3.4
Latin America	0.3	-0.8	1.7	3.4	3.7	1.8	3.3
Brazil	1.4	1.5	2.1	3.3	3.5	2.1	3.2
Mexico	-0.3	0.9	2.5	3.4	3.8	3.2	3.5
<b>EMEA</b>	<b>1.6</b>	<b>1.4</b>	<b>1.6</b>	<b>2.5</b>	<b>2.6</b>	<b>2.3</b>	<b>2.6</b>
Eurozone	1.5	0.8	1.1	2.2	2.3	1.9	2.4
Germany	0.6	0.2	0.5	1.9	2.0	1.5	2.0
France	2.1	1.2	1.2	2.2	2.3	2.0	2.4
Italy	1.8	0.4	1.0	2.1	2.2	1.9	2.3
U.K.	2.1	1.8	2.0	2.4	2.3	2.4	2.3
Eastern/Central Europe	3.5	2.9	3.4	3.8	4.1	3.3	3.7
Russia	5.0	4.3	5.0	5.0	5.0	4.2	4.7
<b>Asia Pacific</b>	<b>1.9</b>	<b>2.6</b>	<b>2.5</b>	<b>3.0</b>	<b>3.2</b>	<b>2.6</b>	<b>2.9</b>
Japan	0.4	0.3	0.5	0.8	1.0	0.3	0.6
Australia	2.7	3.8	3.0	3.5	3.3	3.1	3.0
Emerg Asia (less China)	4.0	5.7	5.1	5.8	6.0	4.5	4.7
China	7.3	8.0	7.5	7.8	7.5	7.8	7.6

**There is considerable global dependence on a U.S. economic upswing which remains limited and near-term due to low capacity use, a swelling federal budget and current account deficits and uncertain business commitments on hiring and capital spending.**

***No excuses... policy settings are to blame***

The prevalence of heightened risk should not serve as an excuse to avoid overdue structural reforms which can promote greater economic opportunities and competitiveness ahead. In some countries domestic demand continues to decline due to very "classic" policy defects. Various factors are significant particularly for the drop in consumption and investment demand, while some of them are more related to a lack of initiative for structural reform than to the impact of world risk agenda:

- The burden of costs on businesses through taxes and social security contributions remains to be too high in many OECD countries. Although a necessary source of revenue for public expenditure, taxes, in particular when levied on labour, may directly reduce employment.
- Enterprises are containing staffing in view of the rising cost of the "labour" factor and the high rigidity of labour markets in some OECD countries. The structural inflexibility of some labour markets has shown particularly painfully. In the case of rigid wage systems, constraints on jobs remain the only alternative for many businesses.
- Plans to invest are being revised due to a lack of confidence in future sales opportunities. Uncertainty, as well as declining expectations of investment returns, gives rise to enterprises putting aside any plans to invest.
- Lack of willingness to invest is often accompanied by financial bottlenecks. The downturn of the stock market raises the cost of capital pushing companies to raise debt/equity ratios (since debt is cheaper with current low interest rates) but which then diverts cash flow into debt service rather than capital investment.
- Human capital is one of the key factors for growth. In view of the current demographic challenges overall employment rates, including for groups that are currently underrepresented, need to be increased to sustain growth. There is an imbalance between the availability of skills and companies' requirements. Lifelong learning and close links between education institutions and the labour market are important to enhance the matching of skill offer and demand.
- Education - including lifelong learning that is the comprehensive provision of purposeful learning opportunities throughout every individual's life - is essential to enable a society to cope with the inevitable shifts and opportunities in the labour market. The quality of pre-school, primary, secondary, tertiary and life long learning educational, including re-skilling, capacity will drive the success of investors in the future.

### ***Save multilateral co-operation***

Multilateral co-operation needs to be reinforced. There is still a threat that political disagreement will spill over into trade relations between major G8 trading partners. Even the Doha Round of trade negotiations has run into shallow water.

### **BIAC urges G8 leaders to renew their commitment to the world trading system as the principal path to growth.**

- The maintenance of a predictable, open and rules-based multilateral trading system has historically been one of BIAC's most important international economic objectives. With the Doha round the stakes for the WTO have never been higher. They involve the future relevance and credibility of the WTO as a renewed engine of global economic growth and prosperity.
- For over 50 years, the disciplines of the GATT/WTO system have made a major contribution to economic growth and improved living standards around the world.
- The world trading system and the open markets that it promotes are essential to sustainable economic growth, supporting and diffusing innovation and technology, and reducing poverty by creating wealth.
- Political differences should not result in self-defeating squabbles that impede the progress of liberalisation. The effects of boycott threats and veiled sanctions from any WTO party are detrimental to the whole economy.
- On this basis, the business community of the OECD member countries continues to support broad-based, balanced, trade negotiations under the WTO "Doha Development Agenda" as a matter of high priority. The G8 has a key role to play in fostering further confidence in and support for the global trading system.
- Our priorities for the Doha negotiations include continued and significant negotiating progress on: Industrial goods; Services; Agriculture; the relationship between trade and investment; Trade facilitation and Transparency in government procurement

### ***Continue pressure on innovation to spur growth***

According to sources such as the results of OECD studies, there is evidence of widening disparities in GDP per capita growth rates across the OECD countries over the past decade.

- Over the 1990s the United States began to pull away from most other countries in terms of GDP per capita levels. There was a significant speedup of productivity growth in the United States around 1995, considered unusual in a country at the productivity frontier in many sectors. In addition to the United States, only a small number of OECD countries have shown improved or continuing good performance in terms of productivity and/or GDP per capita growth.
- There are important gaps between countries in terms of their status and pace of movement along the various dimensions in which the business environment is changing. It would be desirable to centre the OECD analysis of a phenomenon so central to the

economy as the evolution of innovation and productivity squarely within a framework which takes account of each of these dimensions (innovation, flexibility, regulatory quality) and the interactions between them.

- BIAC's membership believes that the diffusion of ICT has been one of the factors playing a major role in driving innovation and growth performance in recent years. According to OECD studies innovation, including the use of information and communication technologies, was the main driver of productivity growth in some countries, but not in others. There is strong evidence that increased use of certain types of ICT equipment over the 1990s was associated with better productivity performance. **The promotion of ICT investment also in SMEs (e-business) and public administration (e-government) must remain high on the agenda of sound economic policies.**
- BIAC would like to draw the attention of governments to the simple but powerful logic stream - that it is innovation which improves productivity, resulting in enhanced living standards through growth. The crucial question that G8 leaders will have to ask themselves is: **what am I doing to enable or inhibit innovation in the context of law, regulation and practice within my purview?**

### ***Good governance for governments and corporations***

High quality regulatory frameworks that promote competition and that do not impede trade and investment should be the goal of all regulatory reform agendas.

- Integrating joined up regulatory policy into the mainstream of government's strategies and actions, thereby contributing to efficient markets and good governance, is an important goal for business. Regulatory Impact Analysis (RIA) and administrative simplification are key aspects of such efforts.
- E-Government shows that this phenomenon is an important enabling tool to reform the way public administrations operate to result in more efficient customer-focused public administration, that is, responsive and adaptive to changing societies and economies. Developing "seamless e-government services" can be an important contributor to administrative simplification and lead to greater efficiency for both government and business.

Good governance is a constant theme not only for governments but also for businesses.

- The essence of corporate governance is to address investor demands to enhance the transparency of and confidence in the performance of companies and to guarantee shareholder rights.
- Every national regulatory system has to find its own balance between regulation by governments and self-regulation. The current structure of national systems of national corporate governance, derived from international instruments as the OECD Principles of Corporate Governance, should be maintained.
- Spectacular business failures in the recent past cannot necessarily be attributed to deficiencies in corporate governance. There are solid regulations in place and some of them have been strengthened very recently, not always for the better.

- In fact, BIAC member organisations have participated actively in the elaboration and revision of national corporate governance systems in the past. Deficiencies can be attributed largely to failures of enforcement, not to the lack of frameworks as such.

### ***Strengthen growth and investment in developing countries***

As foreign direct investment flows have dropped sharply (by two thirds between 2000 and 2002), private financial flows to developing countries have also declined. **BIAC believes, nonetheless, that any sustainable approach to overcoming poverty must include the development of a national private sector as a crucial factor.** One of the focal points of economic co-operation should therefore be the creation and strengthening of a robust private sector in developing countries. Investment promotion activities of the home country, enhancing standards of public governance and fostering the development of the domestic financial sector in the host countries remain important tasks.

Perception counts, and income rules. Economic progress is ultimately constrained when advancement does not permeate all segments of society. A rising tide may lift all boats but not necessarily equally.

- In this regard, infrastructure is paramount, and includes the development of capital markets, roads and mass transportation, water supplies, sanitation and hygiene, housing and education and training. For example, while India gains from its deep technical skills, the economy is slowing due to limited infrastructure. Only 50% of roads are paved in India while 80% of China is paved, which sustains stronger growth and is more likely to diffuse benefits to society.
- Technology exists to monitor and customise efforts to meet specific needs wherever they may be found. Basic education modules in native languages can now be delivered on demand to children and adults in the most remote parts of countries with handheld, mobile devices.
- The emergence of the knowledge economy means there is greater focus upon and recognition of the notion that people and their skills are the key to international competitiveness and sustainable growth. While economic integration, investment, trade and diffusion of technologies support growth, they also induce adjustment by the persons and economies that receive their benefits. A fundamental requirement for addressing these adjustments, which is even more imperative for developing countries, lies with an adequate education system and the availability of training in these basic skills.

**Given the will, governments, companies, and non-governmental agencies can spread global best practices and promote an inclusive standard of living.**

**We look forward to a continuing partnership with the G8 and other OECD governments to engage in our mutual stewardship of the world economy.**