EUROPEAN CENTRAL BANK

EUROSYSTEM

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Summary of the Non-Financial Business Sector Dialogue on 13 November 2019 in Frankfurt am Main

Participants

- Members of the Governing Council of the ECB or their alternates.
- Representatives of ABB Ltd, Air Liquide SA, BASF SE, Borealis AG, Buzzi Unicem SpA, Deloitte, Duisburger Hafen AG, E. ON SE, Euronics International Geie, Ferrovial SA, Ford of Europe GmbH, Grimaldi Group SpA, Ingka Holding B.V, La Doria SpA, Logwin AG, Miele & Cie KG, Nestlé SA, PricewaterhouseCoopers GmbH WPG, SES SA, Securitas AB, STMicroelectronics International NV, The Adecco Group, Volvo Group, Vos Logistics NV.
- Senior ECB officials from the Directorate General Economics, Directorate General Monetary Policy, Directorate General Communications and Directorate General Secretariat, the Counsel to the Executive Board and the ECB's Chief Compliance and Governance Officer.

The ECB President welcomed representatives of the participating companies and reminded participants of the nature of the Non-Financial Business Sector Dialogue as a forum for interaction at the highest level between the ECB and non-financial companies. The dialogue helps to inform the ECB about the business sector's views on the economic situation, and thereby deepen its understanding of economic developments and issues relevant to policymakers. It complements similar high-level dialogues that the ECB maintains with representatives of financial sector institutions. As with these other dialogues, the same high standards of transparency are followed, including publication of the agendas, a list of participating companies and summary minutes.

Outlook for the euro area and the global economy

The discussion focused on (i) the assessment of demand and supply conditions across different sectors, (ii) the effects of trade tensions and geopolitical uncertainty, (iii) the development and outlook for profit margins and the assessment of price pressures, and (iv) medium-term structural challenges for businesses.

On economic activity, most participants considered that growth in the euro area, as well as globally, had been moderate in 2019, although the views of participating companies on the extent of the slowdown, and on the outlook, varied somewhat depending on the main sectoral and geographical focus of their activities. The slowdown was particularly evident in the manufacturing sector, including notably in the automobile sector, which faced a number of longer-term challenges. At the same time, consumer sentiment and spending had held up relatively well, providing resilience to the broader macroeconomic situation. A number of participants referred to recent, tentative signs of stabilising or improving activity. Concern was expressed more in terms of low growth in Europe, rather than in terms of a recession. However, it was emphasised that the outlook remained surrounded by downside risks and was clouded by a high degree of uncertainty.

It was highlighted that businesses continued to be affected by trade tensions and geopolitical uncertainty, which were seen as weighing on the investment outlook in some sectors and regions. In this context, a clear view of the situation ahead for business was considered to be impaired in a number of sectors. Trade tensions between the United States and China were viewed as having caused a reduction in trans-pacific trade. Tariffs had, for some European firms, increased costs that were difficult to pass on. Some investment projects with long lead times would have to go ahead regardless – the shift towards electric vehicles and artificial intelligence were cited as examples. However, a more general trend towards increasing the required local content of production was also identified.

Brexit was cited as a concern by a number of participating companies. Although the risk of a “no-deal” scenario appeared, for the time being, to have receded – it was even suggested that an orderly Brexit could lead to a rebound in activity in the United Kingdom that could also benefit the EU – there was still considerable uncertainty related to possible future disruptions to trade, arising from the introduction of customs processes. Reference was made to businesses having been obliged to increase stocks in the United Kingdom several times in 2019, ahead of deadlines set for the country’s departure from the EU; this had incurred additional warehousing costs. Looking ahead, participants mentioned plans to permanently increase warehouse capacity.

Turning to prices and cost developments: cost pressures – notably on wage growth, especially for higher skilled jobs – were generally seen as being stronger than the dynamics of consumer prices.

A number of participating companies referred to increases in wages, particularly in central and eastern Europe, as well as in Germany. Reference was made to the increase in permanent, as opposed to temporary, employment, which was indicative of a still tight labour market. Labour shortages existed, especially for skilled positions, such as those of engineers. There was an adverse effect on the labour force arising from population ageing in Europe, which – it was suggested – would need to be countered by higher participation rates. Inward migration could also play a role but, in this context, it was considered important to bear in mind the particular need for skilled workers. It was emphasised that the retooling of the labour market also provided an opportunity for growth.

At the same time, participants considered raising prices to be difficult, which consequently squeezed profit margins. Overcapacity and/or strong international competition made it difficult, in many sectors of the economy, to pass on cost increases; consequently, profit margins continued to be contained. This reflected a number of factors, including international competition, dense retailing networks and the increasing role of discounters and online trade. Attention was also drawn to the increase in asset prices, in particular house prices, as a result of which households were seen to be spending more on housing at the expense of consumption.

Despite trade tensions, geopolitical uncertainty and the squeeze in profit margins, participating companies emphasised the importance of undertaking a major technological transformation and investing to improve productivity, particularly in digital technologies and automation. It was also considered essential to invest in improving the skills of the workforce with respect to the needs of digital transformation.

The need to reduce carbon emissions and the transition to a more environmentally friendly economy was viewed as posing further major challenge for businesses over the medium term. The implications of this transition were considered to be widespread across sectors of the economy. Participants saw a need to continue to develop and improve currently predominant technologies as well as new ones in the automotive sector. Participants also perceived risks to the smooth transition of the automotive sector; the need for coordinated infrastructure improvements and incentives for consumers to buy electric vehicles were noted as important, alongside the implementation of regulatory changes. It was also noted that, in the United States, some infrastructure projects supporting the necessary transition were private rather than public, which could provide a model for Europe. New rules will come into force on 1 January 2020, which will significantly reduce permissible sulphur emissions for shipping fleets. Consequently, participants expected fuel prices to rise and shipping costs to increase; it was observed that this might lead to a shift from sea to road transport negatively affecting the environment. Participating businesses also highlighted the challenge for the construction sector, where there was also perceived to be a need to significantly reduce carbon dioxide emissions. Overall, participants felt that the challenges of sustainability would remain a prominent focus for companies in the years ahead, requiring substantial investment and innovation – even as firms are confronted by increasing costs and the need to focus on short term issues, rather than longer-term adjustment. However, it was recognised that obsolescence, triggered by taking into account the cost of externalities that had previously been disregarded, would also generate business opportunities.