Europe in the Global Economy: Matching the U.S.?

Munich Economic Summit 2–3 May 2003

Welcoming Address by

Christian Ude
Lord Mayor, City of Munich

Ladies and gentlemen,
distinguished guests,

In my capacity as Mayor of Munich, I am proud to be able to welcome you to the second **Munich Economic Summit** in our city.

In the light of current developments, maybe I ought to begin my speech by talking about the role of the European cities in promoting peace.

After World War II, nearly 60 years ago, the European continent and its cities lay in ruins. But soon afterwards, the cities of Europe were taking practical steps to bring people together by entering twinning relationships with other cities.

To give an example, the City of Munich has meanwhile developed international partnerships with seven sister cities. On the basis of these relations we are engaged in intensive dialogue and cooperation with international networks like EUROCITIES and the network of the International Union of Local Authorities (IULA).

And, we may say that the cities of Europe have turned out to be engines of growth, innovation and social cohesion in the past decades of the European unification process.

Europe is established and built in the cities, no doubt. More than 80 percent of the EU citizens live in urban areas. And the lion's share of gross value added is generated in cities, showing strong growth potential in the European economy, especially in the service sector.

In order to improve the living conditions of the people and promote the competitiveness of local companies, Munich has invested billions of euros in public infrastructure, such as the new Trade Fair Centre, the new Airport and the extension of public transportation.

Munich is one of the leading business locations in Europe, no doubt. Growth clusters of world-wide importance have settled here in a variety of key branches, like biotechnology/life sciences, information technology, nanotechnology and the media.

In international benchmark reports, Munich has a high reputation due to its famous universities, its highly skilled labour force and research and development facilities. This is one of the main reasons why the relations between US companies and Munich firms are so strong.

Most of the German subsidiaries of US enterprises are located in or around Munich. The exports of Munich firms to the US are strong, the BMW Group, for example, is selling many cars to America, and established a manufacturing plant at Spartanburg.

In the United States, Munich is competing with top metropolitan areas like Boston or Silicon Valley. These US city regions are our benchmark.

The Department of Labour and Economic Development of the City of Munich seeks to promote close connections with prosperous US regions by presenting Munich in the United States as a German Centre of Excellence.

With the 2006 Soccer World Championship to be held in Germany, Munich has seized a unique opportunity to further upgrade its business location and international reputation.

We are doing this by hosting the opening of the Games in the newly built Soccer Arena and making the new Media Centre available for world-wide press activities.

In times of economic difficulties, the capital investments made by the cities should help to overcome the showdown of the economy. Munich, for example, makes great efforts to maintain a high level of capital investment in infrastructure projects, even and especially in times of declining public revenues.

As a precondition for healthy cities, we need a solid financial system, however. A system which helps to make the cities less vulnerable, and provide long-term financial stability. It should be implemented on the national as well as on the European governmental level.

If we and the European Union want to be locations of innovation in years to come, the European Community and national governments should undertake all they can to strengthen the cities and their prosperity potentials. And this would also be a solid strategy to strengthen the competitiveness of the whole continent.

Ladies and gentlemen, I hope this summit will show the way how this present economic crisis can be overcome and how competitiveness can be strengthened on a European level.

In this spirit, please accept my best wishes for a successful conference and fruitful discussions.

Thank you for having come to Munich once again, have a pleasant stay in our city and enjoy these meetings.

Welcoming Address by

HORST TELTSCHIK
Chairman of the Board of Directors,
BMW Foundation Herbert Quandt,

President Klaus,
Prime Minister Medgyessy,
Dear Minister-President Stoiber,
Deputy Prime Minister Šlesers,
Excellencies,
Ladies and gentlemen,

I should like, on behalf of the BMW Foundation Herbert Quandt, to welcome you most cordially to the second Munich Economic Summit in the Bavarian capital. After the successful premier last year, the Summit has become an attractive brand name. The fact that there are 140 participants from 23 European countries speaks for itself, not to forget our American friends and participants.

I would like to thank the Sponsors of this European Summit who have contributed significantly to its success. Their generous financial support deserves special mention in these times when burdens are increasing for the private sector, and the overall level of economic activity is declining.

Ladies and gentlemen, the theme that the two organisers, CESifo and the BMW Foundation Herbert Quandt have given to this year's summit "Europe in the Global Economy: Matching the US?" might be a bit provocative nowadays.

"Matching the US?" – the Summit's subtitle draws attention to both the close economic ties and the global economic competition with the United States. How can Europe increase its competitiveness? Does the American economic model lead the way? Can the Europe of 25 some day match the economic power of the US?

It is quite obvious that the Europeans cannot and will not have the political will to match the military power of the United States. They have just small alternatives to international crisis settlement. Economic power could be a convincing alternative of the Europeans and this would be highly respected by our American partners.

Let me add a personal word: This year, we have had two American ministers visit Germany. The first was Secretary of Defense Donald Rumsfeld, and tomorrow we will welcome Bob Zoellick, the Secretary of Trade, and they both come and came, respectively, to Munich and not to Berlin. We are proud of that. This is hopefully a contribution to improve German-American relations from the Munich territory.

Now in particular, with the end of the Iraq war, Europe has the chance to contribute significantly – together with the United States – to the reconstruction of Iraq and to a peaceful development in the whole region and thus, once again, to put common goals and values in the foreground of transatlantic relations. The free competition of ideas, concepts and products can develop only on the basis of a strong Atlantic partnership.

I hope that we will all find today's and tomorrow's discussions extremely stimulating. The special characteristic of this conference is the mix of economic professors with business executives, politicians and economic experts from the media.

Therefore, it is with great pleasure that Professor Sinn, President of CESifo in Munich and I open the second Munich Economic Summit.

Welcome to Munich, and Professor Sinn you now have the floor.

Introduction by

HANS-WERNER SINN

Professor of Economics and Public Finance
President of the Ifo Institute for Economic Research
and of CESifo Inc.

President Klaus, Prime Minister Medgyessy,
Minister-President Stoiber,
Deputy Prime Minister Slesers, Mayor Ude,
excellencies, colleagues, ladies and gentlemen,

The war is over, tensions have subsided, and it is now clearer than ever that the United States is the world's superpower. Even though the US economy has lost steam in the past few years, US GDP per capita last year still was nearly 50 percent above the EU average, and even in absolute terms it was 10 percent above EU GDP, although US population size is nearly a quarter lower. In this year, the US economy is expected to grow by another 2.4 percent while the EU growth rate is a meagre 1.1 percent, according to ifo projections.

Next year, Europe will have 450 million inhabitants while the US will only have 280 million or so, and still US GDP will be similar to that of Europe.

There must be something special about the US economy that has generated this enormous economic success. What is it?

Is it the common government, the political unification of the continent?

Is it the political power that has helped the US shape the world trading system according to its preferences?

Is it the fact that they have a market economy without an adjective, as Vaclav Klaus has argued?

These are some of the questions we want to discuss at this Summit. I am glad that we have been able to assemble an excellent group of specialists who can provide answers and help clarify the matter.

From my personal perspective, the ultimate goal is to see what Europe can learn from the US to achieve similar productivity growth.

One of the clues might be the capital market, and that is the question to be discussed in the first panel. It is true that, with the introduction of the euro, Europe has established a new capital market for interest bearing assets. The rapid interest-rate convergence that the announcement and introduction of the euro has brought about will reshuffle the savings capital to its most productive uses towards countries that previously were disadvantaged. This will surely boost economic growth in Europe in the next two decades.

However, Europe still does not have good markets for risk capital. Here the US has an outstanding system with its venture capital markets and its stock exchanges, something that is worth imitating in Europe despite the recent cracks that the system has shown. Except for Great Britain, joint stock companies play no particular role in the economies of the continent, and attempts to change this situation, such as the opening of the new market for young joint stock companies in Frankfurt, have failed miserably.

Even more important than the capital market, however, is the labour market. While the US economy has created 40 percent more jobs during the last twenty years, Europe has performed poorly, and its unemployment remained intolerably high. Western Germany has even experienced a shrinkage in the number of hours worked, unable to provide additional jobs for the immigrants who, in net terms, amounted to 6 percent of the west German population. Immigration in Germany, therefore, was immigration into unemployment, even though it was the domestic inhabitants who went into unemployment and the immigrants who took their jobs. Many other European economies have performed better than the German economy, but none has been able to match the US. This is the field where the title of the conference fits best.

I share Vaclav Klaus's view that the reason for the poor European development is indeed the adjec-

tive that we have added to the market economy. It is the social dimension that we have added to the labour market that has caused the problems.
Job tenure laws have increased the power of trade unions and allowed them to carry out an extremely aggressive wage policy. If the customer is forced to buy the product, the seller has all incentives to increase the price.

The welfare state is expensive and requires higher and higher taxes that discriminate against work.

And, what is more, by paying replacement incomes to those who have no jobs the welfare state has become a fierce competitor of the private economy in the labour market that, together with the Asian low-wage competitors in the product markets, takes away the air that the private economy needs to breathe.

I am eager to hear what the speakers in the second panel have to say on this issue.

When we designed the conference we did not know that the conflict between the US and some European countries about the legitimacy of the Iraq war would escalate to the extent it did. Given this escalation, I hope that we will be able to prevent a new cold war in transatlantic political relations. The future of the World Trade Organisation and the challenges for the Doha Round will be intensely discussed in the third panel. In the past, the US has not been overly co-operative when it came to international agreements. This at least is the feeling that most Europeans have when they think of the Kyoto protocol, which the US did not ratify, and the International Court of Justice in the Netherlands to which the Americans do not want to submit themselves. I wonder what prospects our speakers will be able to offer in the area of trade negotiations.

The last panel is on the future of the European Growth and Stability Pact. Matching the US does not quite seem the right title in this context, since the US is likely to have changed its budget by 6 percentage points of GDP, from a surplus of 2 percent to a deficit of 4 percent in only four years (2004). This is the opposite of what the pact requires, which imposes a ceiling of 3 percent on the budget deficit.

However, you will have noticed that we have added a question mark to the title of the conference. This is more appropriate now than ever, because I believe that the Americans are having a problem here. The American households do not save, the American government does not save, but the American economy needs the funds for investment. These have been increasingly coming from abroad, as can be seen by the huge current account deficit in the order of more than 4 percent of GDP, but they will not be coming for ever. There is the risk of a sharp depreciation of the dollar with negative repercussions on world trade, in particular the competitiveness of the European economies. This development is anything but healthy, and here the US should try to match the Europeans instead.

Unfortunately, as you know, the Europeans no longer take the pact very seriously since a number of countries, including France and Germany, will violate it. Minister Eichel has announced that he will borrow 2.8 percent of GDP, and Chancellor Schröder has recommended that local communities borrow another 0.35 percent from the German Bank for Reconstruction and Development. If we add these two numbers it follows that the government has already declared implicitly that it will run a deficit of 3.15 percent of GDP and hence violate the pact in 2003. These are no good signs for Europe either. Let us listen to the experts whom we have invited to speak on this issue in panel 4.

This is all I have to say at this stage. I am sure we will all have an exciting and stimulating two days here in the Bayerischer Hof and in the Residence of Bavaria where Minister-President Stoiber will receive us tonight. I now cede the floor to Minister-President Stoiber and President Klaus, to a lawyer and to an economist, both of whom, I am sure, will have important messages for us, and I thank you for your attention.