

2018 economic perspectives: Onwards and upwards to qualitative growth?

The major economies have had to brave the ups and downs of the international, (geo)political environment throughout 2017 and seem to be on the path of a stable recovery in the mid-term. Whereas the main indicators have turned green internationally and in the Eurozone, why are we still faced with uncertainty? Is Luxembourg an example for the countries of the Eurozone? What will be the determining features of a qualitative growth in 2018? To answer these questions, the Chamber of Commerce is keeping a close eye on the international conjuncture, and Luxembourg's more specifically, thanks to the business executives' assessments of the economic situation by means of the Eurochambres 2018 survey as well as Luxembourg's main qualitative growth drivers.

The international conjuncture: the indicators have turned green but still do not prevent circumspection...

As we draw closer to the end of 2017, a wind of uncertainty blows over the economies. In spite of growth opportunities (over 2% projected in 2017 and 2018 for the United States, an excess of 6,5% over the same two years for China, about 7% for India, a return to a positive 1% growth for Brazil, and Russia inching closer to 2%, whereas the Eurozone will surpass 2% in 2018), we still face numerous risks.

As we witness an international upturn that includes the Eurozone, uncertainties are rising this time from one of the zone's leaders. If Germany, the economic powerhouse of the Eurozone, fails to form a government, the country's administration will be weakened resulting in a delay in the Eurozone negotiations.

At the same time, the European Central Bank (ECB) has announced a decrease in its covered-bond purchase programme as a part of its "non-conventional" policy called Quantitative Easing. It reflects its intention of a "return to a normal" state of affairs. However, this programme has been extended up to September 2018, and could continue beyond then if we were to experience further negative jolts. Contrary to its American counterpart, the ECB does not consider a downturn in its results. As a matter of fact, it forecasts to maintain the interest rates at their current levels over a prolonged period.

As for the Brexit negotiations, they do not seem to be progressing much, and the negotiating counterparts will probably not be able to address the matter of commerce in 2017. Even though a firm and definite Brexit has been declared, the sixth round came to an end on November 10th in Brussels as it added yet another question, pertaining to Northern Ireland, to those which have largely contributed to the lack of progress in the negotiations.

Most of the Old Continent seems to be witnessing a marked growth at the far end of 2017 and could spill over into 2018. That said, the greater uncertainties pertaining to Brexit and certain other political risks could hold back these perspectives.

In Luxembourg, growth is the result of better employment figures alone

The national macroeconomic context is well oriented and can be compared with most of the economies cited above. As per the business survey 2-2017 (*note de conjoncture 2-2017*), GDP growth, in terms of volume, could reach 4% in 2017 and 4.4% in 2018. Throughout the budgetary period, 2017-2021, economic growth is forecast at 3.1%. The figure of 3.1% also approximately corresponds to the expected growth in employment figures between 2017 and 2019 as per the budget drafting authorities. Employment growth should thus continue to progress as unemployment diminishes further. STATEC considers that inflation will stabilise at 1.4% in 2018. These data seem to be positive, but also implicitly presuppose that apparent labour productivity will stagnate after a 15-year period of absence of any improvement in productivity. The central administration also noted that deficit will rise to EUR 890 Million in 2018, which will, however, be compensated by the social security's surplus on the one hand and that of the local authorities. The results thus are only reassuring in appearance.

When social affairs take priority over the economic ones

The Obsevatoire de la Compétitivité (ODC) which recently introduced the new indicators of sustainable development in Luxembourg also analysed its competitiveness, and came to the same conclusion¹. In 2017, across all categories, Luxembourg occupies the 4th place amongst all the Member States of the EU, preceded by Denmark, Sweden and Ireland. This rating by the ODC demonstrates a favourable economic climate on the one hand whilst highlighting structural challenges on the other. In taking the 3 aspects into consideration individually – which are the three pillars of sustainable development - the Grand Duchy comes in at the 7th place from the economic point of view, it stands 1st in social affairs and 9th in environmental matters. Albeit, the topper of European social systems could end up lacking the necessary support in the mid and long terms if the economic facet does not find a correspondingly high rating.

Besides, the “weakest” indicator of the economic aspect is the one pertaining to the lacking economic return of non-financial companies. The aspect measures the ratio of the gross operating surplus (the operating margin) against the turnover. What is worrying is that Luxembourg brings up the rear across Europe with regard to this indicator. Inasmuch as financial return is considered to be the fuel of businesses, and a sustained weakness of non financial companies could expose the sustainability of the very backbone of our economy, viz. SMEs, to risk.

So what do entrepreneurs think ?

The results of the 25th Eurochambres survey (see annexe for more details), which are based on answers provided by no less than 595 respondents in Luxembourg are rather encouraging. A certain optimism can be discerned on behalf of the participating entrepreneurs whilst reading the results pertaining not only to the year 2017 but also their forecasts for the upcoming 2018. Such optimism is however somewhat abated by certain results of the manufacturing sector.

In terms of economic climate, it has taken us 10 years to recover the pre-crisis level of confidence. The companies mostly agree as to the stability of this indicator and nearly a 1/4 of the respondents find that the business climate has improved between 2016 and 2017. This indicator's stability, at a relatively high level dominates the entrepreneurial forecasts pertaining to 2018 even more widely,

¹ <https://www.gouvernement.lu/4263741/publications> and the analysis of the Chamber of Commerce can be found [here](#)

which in its own turn, points towards a certain stabilisation of economic growth in 2018 as the indicator of the business climate is closely linked to the GDP growth rate.

The results fluctuate somewhat from one survey to the next as regards the **exports turnover**, which seem to follow the same route as the **national turnover figures**. The results being stable overall, there are, however, the exports indicator of the manufacturing sector has experienced a fall in 2017. The figures must be considered with some caution as only 211 companies of the panel of respondents are exporters.

Contrary to the forecast, one observes a general drop in **employment** prospects as observed by the participating companies this year. This downturn might continue in the manufacturing industry in 2018 but will rise in the entire economy and the services sector.

As for **investments**, one notes an increased cash balance in the industry and particularly in the service sectors in 2017. In 2018, investments should remain “stable” across all sectors (59.2%) or “rise” (32%). But the construction, hospitality and transport sectors will face some concerns wherein the investments will progress only moderately.

Finally, the **main challenges** that have been highlighted by the Luxembourgish entrepreneurs pertain to the lacking qualified manpower, the labour cost and the internal demand, which are in line with previous years.

The seven essential drivers of qualitative growth

1 – In absolute terms, Luxembourg’s economy has been one of the most productive worldwide. It owes that to the spectacular development of its financial sector on the one hand as well as its ability to position itself whilst being competitive in the new, high-added-value sectors. Besides, Luxembourg has been growing for a number of years, but its performance do hide a disturbing reality for the Grand Duchy. **Labour productivity** has not moved forward since the year 2000.

Thus, growth is essentially due to a continuous surge in workforce. Whereas a higher productivity, the crux of any economy, is the only means of increasing riches without spending any more resources. It allows to set aside a surplus of acquired wealth that is shared between higher salaries, higher profits and lower prices. Its impact is decisive on companies as well as citizens: enhanced competitiveness, higher investment capacity and attractive salaries, to maintain a high quality workforce. The society as a whole, will undergo the following effects: an overall increase in the standard of living and preservation of a model that favours social cohesion, increased government revenues aimed at improving infrastructure and a fall in environmental stress for equal wealth being created.

Various projects led by the Chamber of Commerce seek to “kick start” productivity so as to move from a quantitative growth to a qualitative growth. They range from advocating free trade and Luxembourg’s competitiveness in international markets to supporting companies towards digitalisation and labour 4.0. They aim to see the Luxembourg start-up nation take off, and cater to the needs of a qualified workforce. Simultaneously, their goal is also to guarantee the future of Luxembourg’s social model.

2 – The Chamber of Commerce’s watchwords as regards **free trade** are “to stay on course in spite of a risk of economic decline” Free trade is called into question across the world, by the American government amongst others on the one hand, and European on the other. A qualitative growth in Luxembourg will depend on an effective operation of international trade with its partners. Actually, 83.3% of economic growth originated from external trade in 2016. The BRIC countries, those of

Eastern Europe or even African countries with a strong growth potential are all foreign trade opportunities for exports emanating from the Grand Duchy that will allow economic growth internationally without requiring additional, disproportionate resources in Luxembourg.

To keep up the pace, the Chamber of Commerce seeks to work on four fronts: ensure the viability of the European trade policy, promote the internationalisation of companies, facilitate the geographic and industrial diversification even more, and “do its homework” i.e. handle shortcomings within Luxembourg and in Europe.

3 and 4 - The technical progress is an important driver of the evolution of productivity. One of the important facts in this field is the **digital transformation**, the “enabler” of a more intelligent and interconnected world as well as its repercussions on work. Thus, we evoke the appearance of a phenomenon called **work 4.0**.

The digital transformation is a global phenomenon that revolutionises the business model of companies and competitiveness factors. For the Chamber of Commerce, it will be the key catalyst to successfully transition towards a more qualitative growth. Consequently, Luxembourg must become an “early adopter”. Similarly, the labour market changes that originated from new technologies - we must note Big Data, automation, 3D printing, robotisation, the Internet of Things, artificial intelligence (AI), or even the emergence of the economy of platforms - are all opportunities to enhance the quality of work so as to enable a more qualitative growth. The world of digital work is one where work is flexible and bearer of a surplus of quality of life at work.

The Chamber of Commerce positions itself as a partner of choice so as to enable local companies to overcome the challenge of the digital transition. It raises their awareness as to the stakes and opportunities of digitalisation, by means of numerous conferences, or publishing *Actualité & tendances N°18 - Digital Transformation in business and society*. The House of Entrepreneurship and Luxinnovation have joined forces with the Chamber of Commerce so that the businesses shift towards the digital more rapidly, and the House of Training’s 2018 catalogue is resolutely focussed on this subject.

“Arbeiten 4.0 - Chancen und Herausforderungen für Luxemburg” is a joint survey being finalised to be commissioned by the Chamber of Commerce, the *Chambre des Salariés* and the *Ministère du Travail de l’Emploi et de l’Économie sociale et solidaire*. It aims to analyse what is and what will be work 4.0, and should particularly reveal that employment will not disappear as such, but that the jobs being accomplished are undergoing change. It will be a matter of being able to position oneself in work 4.0, facilitate the acquisition of digital skills and competencies at school and in the ongoing training, to support SMEs in the course of the digital transition, mentor them to be more flexible towards work and help adapt it to each sector and/or company as well as following the European trends as regards fiscal policy, “The Single Digital Market”.

5 - The startups are equally capable of revolutionise an economy. In Luxembourg’s case, they are a valuable asset aimed at diversifying the economy so as to make it more healthy and more resilient.

Today, we can already enquire of ourselves whether Luxembourg is a start-up nation or not. In that field, the Grand Duchy has an efficient institutional mentoring system and is able to attract startups. Luxembourg does however suffer from an entrepreneurial culture that can be improved, it is ranked 13th out of the 27 countries of the European Union in terms of percentage of intended

entrepreneurship². The “House of Entrepreneurship” aims to develop that entrepreneurial culture and help Luxembourg’s entrepreneurs succeed. In 2018 it shall be joined by the “House of Startups”, an “incubator of incubators” located in the heart of the capital.

6 - For the OCDE, “it is essential, in order to boost employment and economic growth as well as fostering social inclusion, to ensure that the offer of skills be adapted and fully put to use, whilst continually developing **the qualifications of the workforce**” That said, the lack of qualified manpower is the main concern for Luxembourg’s entrepreneurs. That being the case for 55.3% of them as expressed in the Eurochambres survey. This issue is confirmed by the worldwide ratings of competitiveness such as the IMD’s on the one hand or surveys pertaining to work 4.0 on the other. The workers’ qualification is one of the major concerns as regards in the context of competitiveness. A qualitative growth will have to involve qualitative qualifications.

The Chamber of Commerce is committed to tackling that specific issue at all levels of ongoing training. It promotes the learning and facilitates it. It raises the students’ awareness towards industry, new technologies and entrepreneurship. The House of Training offers 595 training modules and trains 168 employees and entrepreneurs per day. The Institut Supérieur de l’Économie (ISEC) offers Bachelor and Masters level trainings to professionals, which are aimed at practical skill transfer in business administration and management, as well as promoting entrepreneurship.

7 – Last but not the least, **the sustainable quality of the social model** is and shall continue to be a consequence and a factor of a given economy’s quality, which must aim to serve the well-being. The Chamber of Commerce recently expressed its concern as regards the lacking anticipation of the effects of ageing and the difficulties that the social security will be faced with. In the words of the Conseil National des Finances Publiques, in the absence of new measures, the public debt will surpass 30% of the GDP (government standard) as of 2033, 60% (“Maastricht”) as of 2043, and attain over 160% of GDP in 2060. The main cause being a rise in social benefits (pensions, health, nursing insurance,...) due to the ageing of the border crossing workforce and their approaching the age of retirement on the one hand, and the generosity of the retirement benefits on the other.

In its budgetary notice on the 21st November 2017, the Chamber of Commerce prescribes immediate measures such as the complete or partial neutralisation of the link between retirement pensions and real wage as well as structural measures such as the introduction of a link between retirement pensions and longevity or adapting the maximum amount of pension with an aim to ensure the longevity of the social model.

The overall good results in micro and macro economic terms in Luxembourg hide certain truths that are slightly different from the initial conclusions we might draw. Amongst them, one can find the absence of a genuinely qualitative growth that raises the greatest concern. The global context doesn’t give rise to acute episodes of pessimism or optimism and underlines the need for a stronger and closer-knit Europe to face the decline of international cooperation.

² Bilan compétitivité 2017: Le nouveau tableau de bord de la compétitivité ;
<http://www.gouvernement.lu/4263741/publications>