EUROPEAN CENTRAL BANK
EUROSYSTEM

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Summary of the Non-Financial Business Sector Dialogue on 15 November 2023 in Frankfurt am Main

Participants

- Members of the Governing Council of the ECB or their alternates
- Representatives of ABB Ltd., Acerinox S.A., Cepsa, CMA CGM, ebm-papst Mulfingen GmbH & Co. KG, Euronics International, Ferrovial S.A., Grimaldi Group, Inditex S.A., Mango, Michelin Group, Miele & Cie. KG, Nestlé S.A., PageGroup, PricewaterhouseCoopers GmbH Wirtschaftsprüfungsgesellschaft, Repsol S.A , RIU Hotels & Resorts, Robert Bosch GmbH, Schwarz Dienstleistung KG, voestalpine AG , Volkswagen AG, Vos Logistics
- Senior ECB officials from the Directorate General Economics, Directorate General Monetary Policy, Directorate General Communications and Directorate General Secretariat, as well as from the Counsel to the Executive Board, and the ECB's Chief Compliance and Governance Officer

The ECB President welcomed the representatives of the participating companies and recalled the nature of the Non-Financial Business Sector Dialogue, saying it was a forum that enabled the ECB and non-financial companies to interact at the highest level. The objective of the dialogue was to give the ECB an insight into the view of the non-financial business sector on the economic situation and thereby deepen its understanding of economic developments and issues relevant to policymakers. In line with established practice, the agenda, list of participating companies and summary minutes would be published on the ECB's website.

Outlook for the euro area economy

The discussion focused mainly on the following issues: (i) expectations and balance of risks for business activity and employment over the next year and in the medium-term, (ii) expectations and balance of risks for wage and price growth over the next year and in the medium-term, (iii) the impact of tighter financing conditions on activity and investment and (iv) the implications of structural changes (digitalisation, transition to net zero, fragmentation of global trade).

Participants presented a somewhat subdued outlook for activity overall, which was quite mixed across sectors. On the one side, the low rate of unemployment and the recovery of real disposable income as inflation fell should support consumer spending going forward. On the other side, demand for consumer durables remained weak. Sales of consumer goods that had been in very high demand during the pandemic were always going to experience a period of normalisation, but the ensuing weakness was proving more protracted than expected. Furthermore, the present downturn differed from, for example, that experienced in the wake of the global financial crisis in so far as premium segments, which were largely unaffected then, were among the worst affected now. Several participants in consumer-facing industries referred to downtrading weighing on sales volumes. Furthermore, in parts of the manufacturing sector, activity in 2023 had been sustained by the need to work through order backlogs. As these were now largely dealt with, production cuts were expected. Globally, Europe was lagging Asia and – even more so - the US in terms of growth, but doubts were expressed about the sustainability of current US consumer spending.

Notwithstanding the overall decline in producer prices and the moderation of consumer price inflation over the past year, participants emphasised a myriad of cost pressures. The prices of most raw materials and components, even though they had fallen over the past year, were still well above their 2019 levels and in some cases these past increases had not been passed fully through to selling prices. Electricity and gas prices in Europe were still at multiple levels of those in other parts of the world, weighing on the competitiveness of European firms. Meanwhile, wage growth was strong and remained a risk in the period ahead as, at least according to some participants, unions continued to make very high wage demands. In this regard, the high variability of inflation rates across different countries in the euro area was problematic if the workforce of a firm was concentrated in a country with a much higher-than-average inflation rate.

With respect to financing conditions and investment, as most of the firms represented in the discussion had debt with long average maturities or had locked in fixed rates, the effect of higher interest rates on these firms came, for the time being, mainly through reduced customer demand. At the same time, it was acknowledged that the higher interest rates would feed through to firm financing costs over time. In some cases, higher interest rates were seen adding to short-term cost pressures as suppliers sought to pass their higher interest expenses through to selling prices. Higher interest rates also raised the effective prices of goods purchased via leasing. It was, at the same time, argued that the relevance of interest expenses as a cost variable was diminished relative to high energy costs and to the high, but necessary, cost of decarbonisation, which was a key driver of investment.

A considerable part of the discussion was focused on more structural, medium-term cost pressures. The most important of these was the transition to net zero and, in this regard, differences in approach between Europe and the rest of the world. No one questioned the need to decarbonise, and many saw related opportunities for their business. However, in some cases decarbonisation implied replacing efficient, but CO_2 producing, processes with sustainable but less efficient (and hence more costly) ones. Meanwhile, in some industries, it was difficult to incorporate the cost of greening into prices relative to other products. With respect to energy, there were calls for a more holistic approach in the EU with greater focus on energy security at reasonable prices in the shorter term to free up resources for investment in alternative solutions for the longer term. There were also pronounced criticisms of the EU's approach based on regulation and reporting, as opposed to financing action, which placed greater burdens on firms in the EU than elsewhere. Deglobalisation was a further medium-term cost pressure, with several participants confirming the tendency towards greater strategic autonomy, producing “local-for-local” in order to have more resilient operations, but which then also raised prices for consumers.

Against the background of these significant short- and medium-term cost pressures, most participants did not expect to be able to pass rising costs fully through to prices in 2024. Defending margins therefore needed to be achieved by raising productivity, including the responsible roll out of artificial intelligence type approaches, in particular, and new digital technologies more generally. The upfront investments needed to finance this added, however, to costs in the short-term while benefits would mainly be seen in the medium-term. In this context, scarcity of talent and the need to reskill and upskill the labour force were important challenges. At the same time, some participants indicated that they were reducing unskilled positions and only few participants ruled out employment cuts in their planning for 2024.