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Europe's preference for short-term support for consumption

When comparing Europe to the United States or China, one characteristic of Europe stands out: the willingness of public authorities to prioritise short-term support for consumption.

This willingness shows in the large size of social protection systems, in the choice of free trade and offshoring to countries with low production costs, in strict competition policy, and in strong employment protection.

The result of these choices has been a contraction of industry (since importing is less expensive than producing domestically), weak development of the new technology sector (with strong employment protection and abundant regulation), and underinvestment (with resources absorbed by support for consumption and high tax pressure).

These choices are in fact proving detrimental to consumption in the long run, due to weak growth, underdevelopment of the most productive sectors, weak investment and R&D efforts, and obstacles to the establishment of large consortia.

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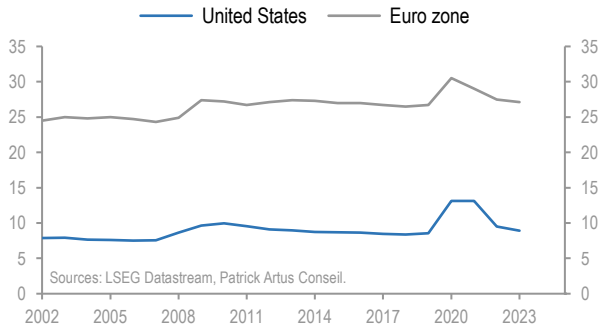
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What characteristics of Europe reveal European governments' preference for supporting consumption?

1. High level of social protection

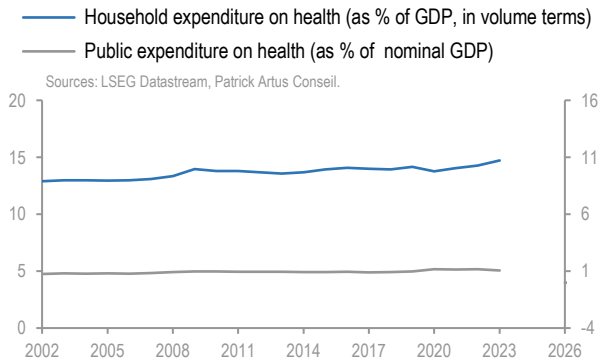
Health and social protection expenditure is much higher in Europe (in the Euro zone) than in the United States. (**Chart 1**).

Chart 1
Public expenditure on health and social protection
(as % of nominal GDP)



In the United States, healthcare expenditure is mainly private expenditure borne by consumers (**Chart 2**), which shows that there is less concern in the United States than in Europe about supporting consumption ex healthcare expenditure.

Chart 2
United States : Expenditure on health



2. The choice of free trade and offshoring

From the outset, the European Union has opted for **free trade**, which it is now finding very difficult to reverse, and only partially (for example, with customs duties on Chinese cars).

This choice stems from the **consumer-friendly model** adopted in Europe, as it **leads to European products losing market share to imported products** (**Charts 3 and 4**), resulting in cheaper prices for consumers due to the low cost of products imported from countries with subdued labour costs.

Chart 3
Euro zone: Manufacturing value added
(volume, as % of GDP in volume terms)

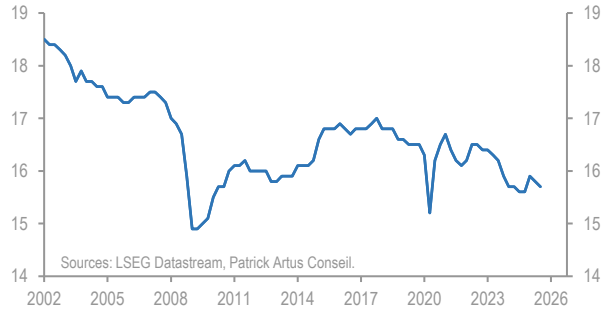
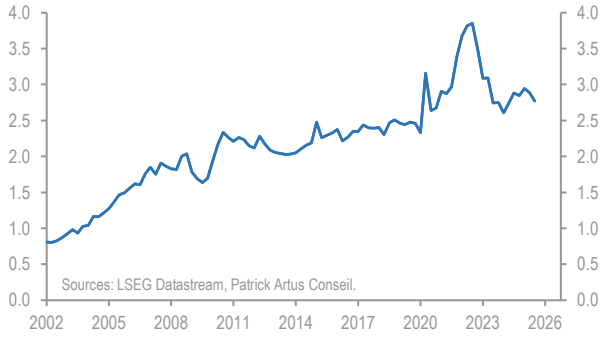


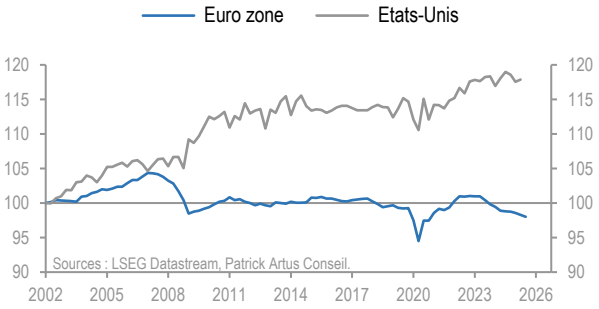
Chart 4
Euro zone: Imports from China (as % of nominal GDP)



3. Strict competition policy

The European Union enforces a much stricter competition policy than the United States, which contributes to lower profit margins than in the United States (**Chart 5**) and is beneficial to consumers in the short term by preventing the emergence of monopoly rents.

Chart 5
Ratio between GDP deflator and unit labour cost
(2002.Q1 = 100)



4. Strong employment protection

Employment protection, as measured by the OECD (**Table 1**), **is strong in the Euro zone**.

Table 1: Strictness of employment protection* (2019)

Strictness of employment protection	France	Germany	Spain	Italy	United States
Individual and collective dismissals (regular contracts)	2.68	2.33	2.43	2.86	1.31
Collective dismissals	3.25	2.61	2.43	3.19	1.33
Individual dismissals (regular contracts)	2.45	2.22	2.43	2.72	1.30
Temporary contracts	2.58	1.67	2.47	2.82	0.27

Sources: OECD
(*) Scale from 0 to 6, with values increasing with the degree of stringency of regulation

This strong employment protection aims to **reduce the risk of redundancy and the precautionary savings that could result from it**.

However, paradoxically, Europe has a significantly higher household savings rate than the United States (**Chart 6**).

Chart 6
Household savings rate (as %)



The result of this policy to support consumption

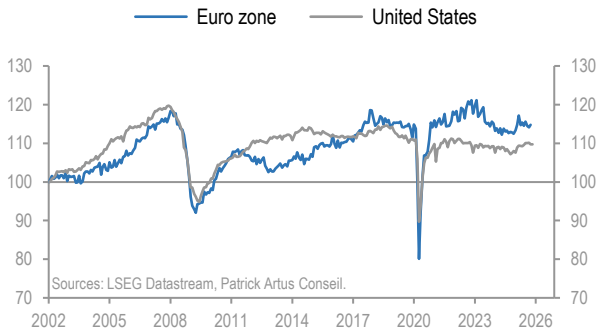
Economic policies in Europe are all aimed at supporting consumption through:

- High social welfare spending;
- Free trade and offshoring, which have contributed to the import of cheap goods produced in emerging countries;
- Strict competition policies;
- Strong employment protection, which limits the risk of redundancy and protects household income.

Unfortunately, these choices have contributed to:

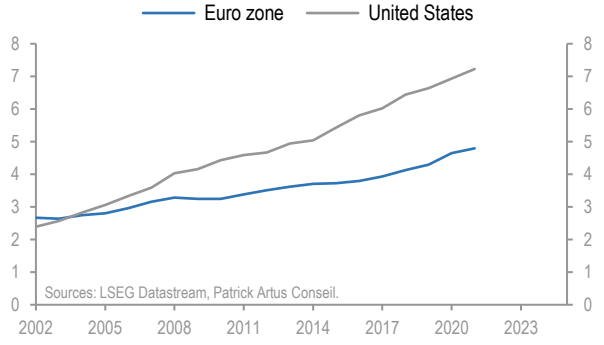
- **Deindustrialisation** (since importing is less expensive than manufacturing domestically), **Chart 3 above, Chart 7;**

Chart 7
Manufacturing production (2002.M1 = 100)



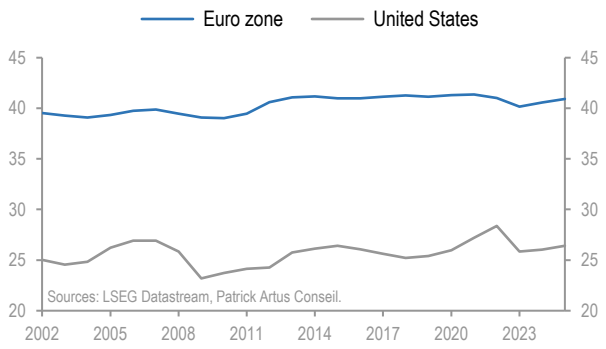
- **The weak development of the new technology sector** (**Chart 8**), with strong employment protection blocking employee mobility in the labour market due to the importance of regulations;

Chart 8
Gross value added of the ICT sector
(as % of real GDP)



- **High tax pressure** to finance the social model (**Chart 9**);

Chart 9
Tax burden (as % of nominal GDP)

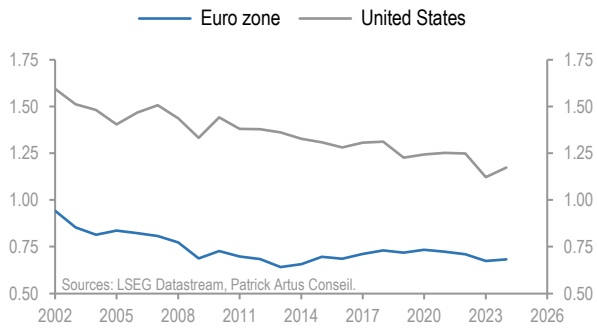


- **Underinvestment** (**Chart 10**), particularly in new technologies (**Chart 11**), with high tax pressure and the concentration of public spending on social expenditure;

Chart 10
Investment of corporations
(in value terms, as % of nominal GDP)

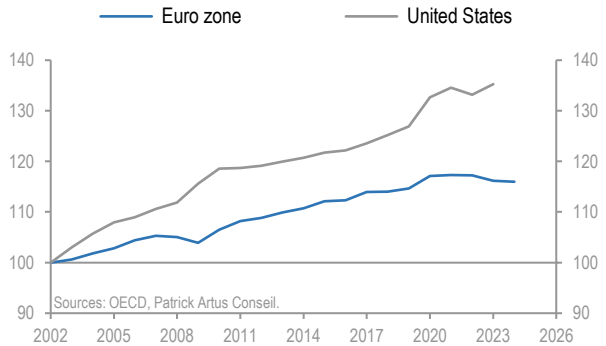


Chart 11
ICT investment excluding software
(in value terms, as % of nominal GDP)



- **Low productivity growth** (**Chart 12**), with underdevelopment of new technologies, underinvestment.

Chart 12
Real labour productivity per hour worked (2002.Q1 = 100)



Summary: in Europe, consumption is buoyant in the short run but not in the long run

The economic policies pursued in Europe (generous social protection, free trade and offshoring, strict competition rules, strong employment protection) **certainly support consumption in the short run** (by distributing significant social benefits, lowering prices through large-scale imports from countries with subdued labour costs, preventing monopoly positions, and protecting employees from the risk of unemployment) **but they have depressed long-term consumption** due to the weakness induced by policies on productivity gains and growth, the underdevelopment of the most productive sectors, underinvestment due to the concentration of public spending on social benefits, and obstacles to the establishment of large consortia.

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