An Action Plan for Europe 2020

Strategic Advice for the Post-Crisis World

the Lisbon council

making Europe fit for the future

Lisbon Council Policy Brief

An Action Plan for Europe 2020

Strategic Advice for the Post-Crisis World

Introduction **Ann Mettler** Foreword **Wim Kok** Education, Skills and Employment **Andreas Schleicher** Turning Indicators into Action **Enrico Giovannini** The Innovation Imperative **Martin Schuurmans** Getting the Macro Right **Alessandro Leipold** Towards a Sustainable Society **Harry Verhaar** Social Innovation **Geoff Mulgan** Europe in the Digital Age **Žiga Turk** The Innovation Imperative **Martin Schuurmans** New Waves of Growth **Mark Spelman** Entrepreneurship **Sören Stamer** Europe and the World **Parag Khanna** Introduction **Ann Mettler** Education, Skills and Employment **Andreas Schleicher** Foreword **Wim Kok** Turning Indicators into Action **Enrico Giovannini** The Innovation Imperative **Martin Schuurmans** Getting the Macro Right **Alessandro Leipold** Towards a Sustainable Society **Harry Verhaar** Social Innovation **Geoff Mulgan** Europe in the Digital Age **Žiga Turk** The Innovation Imperative **Martin Schuurmans** New Waves of Growth **Mark Spelman** Entrepreneurship **Sören Stamer** Europe and the World **Parag Khanna** Introduction **Ann Mettler** Foreword **Wim Kok** Education, Skills and Employment **Andreas Schleicher** Turning Indicators into Action **Enrico Giovannini** The Innovation Imperative **Martin Schuurmans** Getting the Macro Right **Alessandro Leipold** Towards a Sustainable Society **Harry Verhaar** Social Innovation **Geoff Mulgan** Europe in the Digital Age **Žiga Turk** The Innovation Imperative **Martin Schuurmans** New Waves of Growth **Mark Spelman** Entrepreneurship **Sören Stamer** Europe and the World **Parag Khanna** Introduction **Ann Mettler** Foreword **Wim Kok** Education, Skills and Employment **Andreas Schleicher** Turning Indicators into Action **Enrico Giovannini** The Innovation Imperative **Martin Schuurmans** Getting the Macro Right **Alessandro Leipold** Towards a Sustainable Society **Harry Verhaar** Social Innovation **Geoff Mulgan** Europe in the Digital Age **Žiga Turk** The Innovation Imperative **Martin Schuurmans** New Waves of Growth **Mark Spelman** Entrepreneurship **Sören Stamer** Europe and the World **Parag Khanna**

Authors:
Enrico Giovannini, Parag Khanna, Wim Kok, Alessandro Leipold, Ann Mettler, Geoff Mulgan, Andreas Schleicher, Martin Schuurmans, Mark Spelman, Sören Stamer, Ziga Turk and Harry Verhaar

The Lisbon Council would like to thank the European Commission's Education, Audiovisual and Culture Executive Agency for its support. With the support of the European Union: Support for organisations that are active at the European level in the field of active European citizenship.

Introduction
If Not Now, Then When?

by Ann Mettler

Ann Mettler is executive director of the Lisbon Council.

For nearly three years, Europe has been consumed with crisis management and setting up new structures to underpin a better economic governance system. While these reforms were certainly necessary in the wake of the ongoing financial crisis, it has had the unfortunate side effect that other important issues, such as how to bolster drivers of sustainable economic growth, kick-start job creation, sustain a leading edge in innovation and align budgets to purported policy goals have seemingly fallen off the list of political priorities.

With political leaders and the media utterly preoccupied with every minutia of the debt crisis and its institutional and political repercussions, it is perhaps not surprising that last year's launch of the Europe 2020 Strategy went virtually unnoticed. Hard to believe but it has had even less cachet than its predecessor, the ill-fated Lisbon Agenda. The low-key launch is now causing some confusion as plans for an entirely new Competitiveness Pact have emerged, seemingly unconnected with the Europe 2020 agenda, which itself is supposed to be the EU's economic development blueprint for the coming decade. And once again, instead of focusing on implementing a strategy that has been painstakingly negotiated and agreed by all 27 member states, our attention is diverted towards designing another plan that is supposed to shore up competitiveness. But if recent history has taught us anything, it is that one cannot fight economic decline with process. It can only be fought – and won – with action and commitment; with strategy and endurance; with vision and united strength. At some point, Europe has to do what it purportedly set out to do, and I can think of no better time than today, right here and right now.

It is in that spirit that the publication you hold in your hands was conceived. It is a collection of essays by extraordinary individuals who have brought about real change in their field of activities and disciplines. They are doers and innovators, practitioners and experts. The themes are purposefully wide-ranging, reflecting the broad and interdisciplinary nature of the Europe 2020 strategy. The foreword by Wim Kok, former prime minister of the Netherlands and author of the Kok report on the midterm review of the Lisbon Agenda, sets the scene perfectly for the ensuing articles, putting the current crisis in a global context and reflecting on some of the key lessons to be drawn from a decade of experience with the Lisbon Agenda.

> 'One cannot fight economic decline with process. It can only be fought – and won – with action and commitment.'

One cannot overstate the importance of coming months and years in safeguarding our prosperity, our values and our place in the world. The Europe 2020 Strategy will be key in delivering the sustainable growth, employment and innovation we need, and we hope that the reflections, actions and recommendations on the coming pages will serve as an inspiration to pro-actively build and design a better future.

Table of Contents

Foreword
Europe 2020 – Then, and Now

By Wim Kok

Wim Kok is former prime minister of The Netherlands.

The discussion about Europe 2020 and the plans for a new Competitiveness Pact need to be looked at against the backdrop of a world that is changing at record speed. The rise of new economic powerhouses will continue, and many countries and regions around the globe will have to grapple with political uncertainties. Will today's struggle for democracy and liberty in the Middle East take hold or not? Can China's centrally planned economy be reconciled with economic freedom? While it is of course impossible to predict what the world will look like in 2020, one assumption can be made with near certainty: individual countries of the European Union, even the large ones, will be less relevant at a global level.

Only united, focused and concerted action to raise the European Union's economic game, with the help of the Europe 2020 strategy, would make a profound difference in mitigating the otherwise inevitable reduction of global influence, both economically and politically. Sadly enough, current developments do not seem to suggest that Europe will be able to meet this challenge easily. Put simply, the European spirit is not what it was 10 or 15 years ago. New efforts are urgently needed therefore if Europe wants to organise itself in a way that would sustain our global standing and rebuild trust and confidence. This is a crucial moment for European and national leaders to rethink what needs to be done and how to do this.

Comparing the situation today to 2004, when I was in charge of producing a report on the midterm review of the Lisbon Agenda, the situation is much more serious, mostly because of the aftermath of the financial crisis.[1] Even though the crisis didn't originate here, it has had a profound impact on Europe and has forced many issues to the fore. Budget deficits in most countries have reached unsustainable levels, while a lack of competitiveness and lagging

'We need to stop thinking only of what is necessary as a last resort, and instead do what is necessary for our people to become masters of their own future.'

productivity has created serious imbalances. As I know from my own experience as both a prime minister and finance minister, high debt levels can be dealt with as long as a country is able to generate a level of sustainable economic growth of about 2-3% a year. While some countries in Europe will manage to achieve such growth rates, others will probably not. It is this divergent growth path within the EU in general and the eurozone in particular that has become extremely worrying.

Then, as now, there appears to be a structural lack of connectivity between what is said in Brussels and what is perceived as being urgent in the member states. I remember when I was finance minister in the early 1990s, when the Netherlands had to reduce its public deficit to meet the Maastricht criteria. Unpopular measures had to be taken, even in social security, which was particularly hard for me given my background as a trade unionist. I made sure, however, that I never blamed Brussels for these policy decisions, but explained again and again that these measures were good for the country because a delay or even absence of reform would put too heavy of a burden on future generations.

I believe that this approach is still relevant today. Of course European leaders have the right to disagree with one another and to pursue their own national interests, but they have a joint responsibility to move Europe forward as well; to focus not only on immediate crisis management but also on long-term challenges, be it the ageing of our society, the decline in competitiveness or reining in public spending.

Against this backdrop, one of the key issues on which the Europe 2020 strategy needs to urgently focus is facilitating a better, more coherent link between what citizens in member states consider to be in their interest and the priorities of the EU agenda. Until now, all European agendas have been seen as too abstract and isolated to be in the national interest. This is not only because European institutions seem very removed from the lives of most citizens but also because the communication effort has utterly failed.

If you consider, for instance, the long time horizon – 2010 for the Lisbon Agenda and 2020 for the Europe 2020 strategy – it is understandable that most people lose interest. It would be preferable to make it more explicit that a strategy for the year 2020 also tackles immediate issues, and in particular focuses on three challenges which for me are very much part of an interconnected triangle.

First, the need for financial solidarity, meaning that joint efforts to ensure the sustainability of the euro and the eurozone are seen as being in the self-interest of the EU's stronger economies as well. Establishing a properly functioning European Financial Stability Facility (EFSF) falls under this priority. Second, we need stricter rules for the Stability and Growth Pact to ensure the responsible handling of public finances. And third, we need a much greater commitment to shore up competitiveness, also with the help of the Europe 2020 strategy.

But these are not unique insights or new revelations. We have always known that implementation was Europe's weak spot, so the question of enforcement is key. One of the best ways to compel countries into action is by naming and shaming, but that has been, and continues to be, highly controversial in many member states. On balance, one must conclude that the member states have until now not demonstrated a real ability or political appetite to monitor their own performance. The European Commission could of course perform this role, but it does not have an unmitigated track record of success in this area either. In order to enhance its credibility, it might be worthwhile to consider including external and independent experts in its assessments.

If I have one piece of advice for European leaders it is the following: the best way to deal with difficult, interconnected issues is to be as forward-looking and open-minded as possible. If you consider, for example, the outlook for the global economy, and the rise of the new economic powerhouses, then it is necessary not only to protect our current position in a defensive manner but also to work pro-actively towards a better future. This can mean shifting budget priorities around, so that leaders have the financial resources to invest in areas where tremendous benefits can be reaped from a first-mover advantage, for instance in eco-innovation. Or it can mean being courageous and tackling necessary social and economic reforms. If we enact active labour market policies today, or raise the retirement age commensurate with our increasing life expectancy, we can save ourselves a lot of problems in the future

For those who say that countries don't have the luxury of being forward-looking, I say, consider the alternative. We need to stop thinking only of what is necessary as a last resort, and instead do what is necessary for our people to become masters of their own future. People deserve to have an active stake in their society; and they deserve to be told of future challenges that need to be tackled now if we hope to sustain our way of life for future generations.

This is a moment when we have to take an honest look at ourselves and realise that many people are simply fed up; they are fed up with ever more summits and nice speeches; they are fed up with the lack of implementation. People in Europe used to think that they would leave behind a better future for their children. Generally speaking, that is less often the case. There is a prevailing feeling both among citizens and political leaders that a plateau has been reached in terms of social achievements and rights, and clinging on to that status quo has made people too often fearful, defensive and protectionist.

We must realize that the future can also hold many opportunities; that we can be relevant and sustain many of our achievements if we shore up our competitiveness; that we need to organise ourselves better at the European level, driving forward an understanding that there is no inherent contradiction between the national and European interest. And this necessitates that the Europe 2020 strategy has a credible governance and implementation strategy; that it is able to connect the present to the future; and that it is not isolated from the day-to-day priorities of our citizens in this post-crisis world.

1. Wim Kok et al., *Facing the Challenge: the Lisbon Strategy for Growth and Employment: Report from the High-Level Group* (Luxembourg: European Union, 2004).

Skills, Education and Employment: Europe's Next Frontier

By Andreas Schleicher

Andreas Schleicher is director of the Programme for International Student Assessment (PISA)[1], education policy adviser of the secretary-general of the Organisation for Economic Co-operation and Development (OECD) and a member of the Lisbon Council's Board of Advisers. He writes here in a personal capacity.

The case for a better skills policies is clear. Never before have skills been as central to the prosperity of nations and better life chances for individuals as today.[2] Skills contribute to economic growth directly through increased productivity[3] and indirectly by creating greater capacity to adopt new technologies and ways of working and spurring innovation.[4] Up-skilling plays a key role in countering earnings inequality. Adult education and training have a significant impact on both worker productivity and wage levels.[5] Conversely, poorly skilled people, skills shortages and mismatches are increasingly costly (see Figure 1).

One of the reasons why skill shortages often do not translate into better learning outcomes is the lack of a common language through which skills are identified, recognised and communicated from those who use them to those who produce them. Resulting skill mismatches can occur at both the individual level – when a worker would be more productive in another position – as well as at the aggregate level – when there is a general surplus or shortage of specific skills. Both lead to high

> 'Never before have skills been as central to the prosperity of nations and better life chances for individuals as today.'

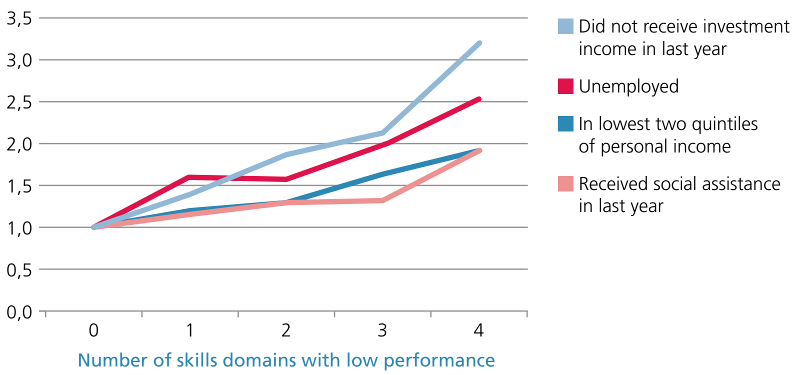
economic costs. Skill mismatches are sometimes caused by ineffective signalling of labour market demands to education and training providers and to individuals, but they are often also the consequence of a lack of responsiveness on the part of education and training providers to information about skills demand.

The transition to a low-carbon, environmentally sustainable economy also belongs to the drivers of the changes in the mix of skills that countries require. But, even beyond that, labour markets are becoming increasingly complex and dynamic. Today, labour markets are characterised by growing convergence of occupational sectors and rising job and occupational mobility, and rapid decreases in the lifetime of domain-specific knowledge. All of this requires individuals to upgrade their skills more regularly to adapt to changing patterns of work and learning. It also requires better data on skills and changing skill demands within existing jobs and changing aggregate skill demands resulting from shifts in the occupational composition.

OECD evidence shows that skills are unequally distributed within our societies and substantial numbers of people do not even reach minimum levels of basic skills.[6] Furthermore, while some countries have managed to

Figure 1: How Lack of Foundation Skills Translates into Economic Disadvantage

Adjusted odds ratios showing the risk of experiencing economic disadvantage, by number of foundation skill domains with low performance, adults aged 16 to 65



Source: Adult Literacy and Lifeskills (ALL) Survey, 2003-2007
Odds are adjusted for age, gender, education, parents' education, and labour force, occupational, income, immigrant and language status.

improve their skill base over time, others have stagnated or even declined. Avoiding the waste of talent requires ensuring access to education for all, both to attain the right level of initial education and to maintain the possibility of upgrading and extending skills over a lifetime.

With a rapidly rising demand for skills, countries can no longer rely on education and training systems that sort individuals. Put simply, countries – including those in Europe – need to improve their skill base throughout the population and capitalise on the full potential of all individuals. This requires governments to ensure that skills are developed in effective and efficient ways through lifelong and life-wide learning, and to ensure responsiveness, quality and flexibility in provision. To achieve this, policies need to do better at meeting the individual needs of people wherever they learn, to look into new ways to take learning to the learner and to examine new forms of educational provision. There is also need for a more appropriate mix of academic and vocational programmes that reflect student preferences and employers' needs, with vocational training providing immediate employability and basic transferable skills to support occupational mobility.

The basis for developing talent and building a skills pool remains acquisition of cognitive foundation skills. Literacy and numeracy are especially important tools for continued learning and for developing more advanced and specific types of human capital (see Figure 2).

Making optimal use of existing skills and preventing attrition of skills due to lack of use and inactivity is as important as producing the right skills. Economic losses arise from a sub-optimal utilisation of skills – in other words, from a mismatch of individuals' skills and skills requirements in the labour market. OECD evidence suggests that skills are developed, sustained and even lost at various stages of life depending on whether those skills are trained, used or neglected at work or home through education and training.[7] Not using skills at all in case of unemployment or underemployment can lead to skills atrophy and a diminishing stock of available skills in people.

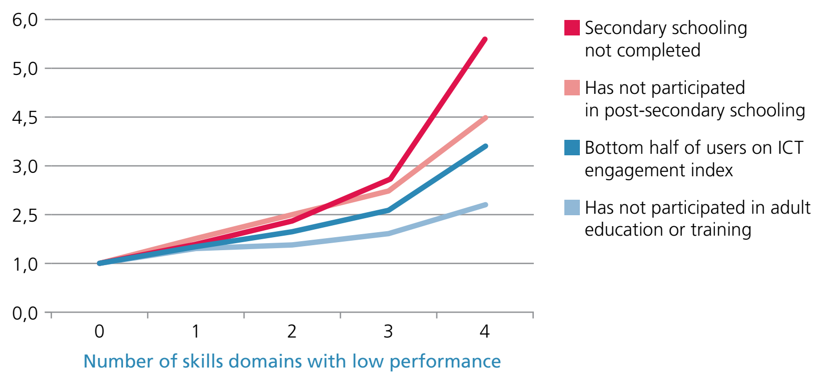
Policies can assist in improving the match of skills demand and supply by establishing national assessment and qualifications frameworks to ensure transparency and systems for recognition of non-formal and informal learning and experience as well as of foreign diplomas. Availability of data and evidence and the use of labour market information for students, parents, employers, government, and education providers – for instance through career guidance – are tools to improve the match.

Targeted policies will be needed in support of groups that are marginalised in the labour market. The integration of immigrants and minorities into the labour market remains an issue of major concern in many countries. School drop-outs represent another group at risk. Key policy actions for this group include early interventions to support young people at risk of leaving the education system without a recognised qualification as well as measures to assist young people in finding jobs and measures aimed at removing the barriers to entry in the labour market. To activate older workers, coordinated policies are needed too, including reforming pension schemes, increasing the retirement age and introducing age-discrimination legislation. But encouraging greater investment in training of older workers is also imperative. Last but not least, women represent the largest underutilised human capital pool in OECD countries. Over the past decades, female educational achievement has increased significantly and, for the younger cohorts, it has overtaken that of men. Over the same period of time, female labour force participation rates have increased but the gender gap remains substantial: on average in OECD countries, only about 60% of women are employed or looking for work compared with 80% of men.

In many countries, skills policies are still piecemeal. Significant gains can be achieved by joining efforts at all levels and investing tight public budgets effectively and efficiently. There is need for a coordinated "whole of government" approach that involves different stakeholders, in particular the social partners, in the design, delivery and

Figure 2: Number of Cognitive Foundation Skills Domains with Low Performance and Human Capital Acquisition

Adjusted odds ratios showing the risk of experiencing disadvantage in human capital acquisition, by number of foundation skill domains with low performance, adults aged 16 to 65



Source: Adult Literacy and Lifeskills (ALL) Survey, 2003-2007
Odds are adjusted for age, gender, education, parents' education, and labour force, occupational, income, immigrant and language status.

funding of skills systems. As the boundaries between the place where individuals learn and the location where they use their skills becomes blurred, governments will need to build new relationships, networks and coalitions between learners, providers, governments, businesses, social investors and innovators that bring together the legitimacy, innovation, and resources that are needed to make lifelong learning a reality for all.

Governments will also need to evaluate the mixture of learning providers (public, private, and third sector organisations) and individuals who provide content, learning opportunities, and instruction to learners of all ages, as well as the ways in which countries can make investing in learning cost-effective for individuals and their employers. This can happen by setting public funds for training for those out of work to incentivise learning or through regulation and taxation to encourage financial institutions to develop new financial instruments that allow learners to access opportunities when they need them most. This includes finding ways to encourage both employers and students to participate in workplace training, to ensure that such training is of good quality, with effective quality assurance and contractual frameworks for apprentices. It also includes engaging employers and unions in the design and provision of vocational training and providing career guidance accessible to all, informed by knowledge of labour market outcomes.

The rising demand for skills also implies that all stakeholders must be prepared to mobilise more time and money for learning. The mixed provision of lifelong learning may demand new funding models to make it easier to invest in learning. Investment in learning needs to be cost and tax-efficient for individuals and their employers. For those out of work, funding needs to be accessible to support and incentivise learning. Governments can use regulation and taxation to encourage financial institutions to develop new financial instruments that allow learners to access opportunities when they need them most, including through lowering cost, reducing risk and smoothing repayments. For learning beyond universal education, education and training systems need to find ways to share the costs among government, employers and students based on the respective benefits obtained.

The OECD has set out to tackle many of these issues through the development of a Skills Strategy that seeks to assist countries in improving economic and social outcomes through better skills and their effective utilisation.[8] The Skills Strategy will build on the Programme for International Assessment of Adult Competencies (PIAAC), a first-of-its kind international survey to measure how the availability of key competencies in the adult population, together with their effective utilisation, translates into better life chances for individuals and nations.

Strong and shared growth increasingly depends on the capacity of nations to anticipate the evolution of labour demand, promote skills acquisition, ensure equity in access to learning, deploy talent pools effectively, make sure the right mix of skills is being taught and learned, give workers the opportunity to adapt their skills throughout their working life, and develop more efficient and sustainable approaches to the financing of learning and training, including identifying who should pay for what, when, where and how.

1. OECD, *PISA 2009 Results: What Students Know and Can Do* (Paris: OECD, 2010).
2. See Chapter A of OECD, *Education at a Glance 2010* (Paris: OECD, 2010).
3. Guido Schwerdt and Jarkko Turunen, *Changes in Human Capital: Implications for Productivity Growth in the Euro Are* (Münich: Ifo, 2007) find that the contribution of labour quality (i.e. educational attainment and labour market experience) to labour productivity has increased over time, accounting for up to one-fourth of euro area labour productivity growth. See also OECD, *Growth Project* (Paris: OECD, 2003); Barbara Sianesi and John van Reenen, "The Returns to Education: Macroeconomics," *Journal of Economic Surveys*, vol. 17(2) 2003; Eric A. Hanushek and Ludger Wößmann, *How Much Do Educational Outcomes Matter in OECD Countries?* (Massachusetts: National Bureau of Economic Research, 2010); Serge Coulombe and Jean-François Tremblay, "Literacy and Growth," *The B.E. Journal of Macroeconomics*, vol. 0(2) 2006.
4. OECD, *The OECD Innovation Strategy: Getting a Head Start on Tomorrow* (Paris: OECD, 2010); OECD, *Skills for Innovation and Research* (Paris: OECD, 2011).
5. OECD, *Promoting Adult Learning, Education and Training Policy* (Paris: OECD, 2005); OECD, *The OECD Employment Outlook 2004* (Paris: OECD, 2004).
6. OECD and Statistics Canada, *Learning a Living: First Results of the Adult Literacy and Life Skills Survey* (Paris: OECD, 2005).
7. ibid..
8. OECD, *Towards an OECD Skills Strategy* forthcoming.

Turning Indicators into Action: Getting It Right This Time

By Enrico Giovannini

Enrico Giovannini is president of the Italian National Institute of Statistics (ISTAT). He previously served as chief statistician of the Organisation for Economic Co-operation and Development (OECD). He is a member of the Lisbon Council's Board of Advisers.

What made the European Union's Lisbon Strategy different from the run towards European Monetary Union (EMU) during the 1990's? The question is far from being irrelevant. In fact, while EMU will be indeed remembered by historians as one of the most successful political processes in the world, the Lisbon Strategy has long been considered a failure. In both cases, there were clear objectives shared by all political parties, strong political commitment and support from public opinion. Actually, one could say that the consensus on the need to strengthen economic growth, maintain social cohesion and respect the environment in Europe was even higher than the agreement on the need to create a common currency. So what was different?

We could spend a lot of time discussing all possibilities, but one difference is quite clear. The efforts made by candidate countries to get into the EMU was focused on a few targets, measured through statistical indicators that could be easily understood by people and actually used by several governments to measure progress towards the target (3% for public deficit, inflation rate, etc.). But the Lisbon Strategy was supposed to be monitored by a plethora of indicators agreed by a group of experts without a serious engagement of stakeholders, unstable over time, kept hidden to public opinion in some countries and rarely used in public communication and national debates.

As the Nobel Prize Winner Amartya Sen once said, "to discuss about indicators is a way to discuss about the ultimate goals of a society." Indicators are particularly valuable if they are shared and used by all parts of society to assess progress towards targets and evaluate the success or failure of policy makers. In a world where we are bombarded by data every day, as demonstrated by hundreds of initiatives around the world, statistical indicators chosen through the involvement of stakeholders and shared by all components of the society can play a crucial role in improving policy making and increasing accountability, especially when they deal with the final outcomes that matter to people.

'Indicators must be as close to people and as well and regularly used by media as possible to make them central in the public discourse.'

The whole debate on "Beyond GDP" is about this issue. Indicators that do not relate to people's lives are seen as irrelevant or, even worse, unfaithful descriptions of what is happening, undermining democratic debates and pushing citizens away from politics. On the contrary, indicators that can be understood and seen by a society as a shared vision of where it wants to go (as when José Luis Rodriguez Zapatero indicated that his target was for Spain to reach a value of GDP per capita higher than the Italian one) can represent a booster for policy reforms.

Of course, indicators *per se* are not the panacea of all policy problems, but they represent a key ingredient of long-term policy programmes like Europe 2020.[1] Therefore, it is important to learn from past mistakes and be sure that indicators are turned into action at all levels. In this perspective:

- It is not enough to compile "league tables" based on a list of indicators chosen at the end of long negotiations aimed at making all countries happy, i.e. relatively easy to achieve;
- It is not enough to share indicators among the "usual suspects" (i.e. policy experts) without reaching out to citizens;
- It is not enough to choose only "input" indicators to monitor policies (for example, the ratio between R&D expenditures and GDP) without any link to the final outcomes relevant for people.

In the case of EMU, which was seen as a financial issue, it was justified to use indicators that could represent economic convergence and stability of public finance. But for an ambitious, all-encompassing strategy like Europe 2020, indicators must be as close to people as possible, as widely disseminated as possible, as shared by stakeholders as possible, and as well and regularly used by media as possible to make them central in the public discourse. Only in this way can indicators play the role they are supposed to play, i.e. to assess progress towards targets.

This does not apply just to the Europe 2020 strategy, but also to other EU policies. For example, a strong proposal has been recently advanced as part of the new cohesion policy currently under discussion. The proposal is to focus the process of setting targets and monitoring using outcome indicators discussed and agreed at national level with the broadest possible engagement of stakeholders.

Outcome-based indicators are clearly one of tools for improving the functioning of democracy and policy making, as can be seen in several "political choice" models based on game theory. For starters, indicators can help in reducing the information asymmetry

between voters (the principals) and politicians (the agents) which lead the latter to implement the most convenient policies for them, and not necessarily the policies sought by the former. These models demonstrate that an election system alone is not enough to select the best politicians, while the possibility for citizens to observe, through indicators, the outcome of policies can be a key tool to help them select the best politicians. In this sense, indicators are clearly vital to the functioning of democracies in the information age.

Of course, indicators can be used for propaganda, but this is why they should be widely disseminated to all stakeholders and used in public debates. Statistical offices in charge of producing indicators should be protected from political interference. The selection of indicators should be made through open consultation of the different components of society (as the UK is doing to select the dimensions of well-being most relevant to citizens). Indicators to monitor strategies like Europe 2020 are too important to be seen as a tool for experts. They should be seen as a key part of the strategy.

Eric Schmidt, the chairman and former CEO of Google, once said a day will come when people will use the Internet to evaluate how parliamentarians voted on proposed legislation, assess the outcome of those laws through statistical indicators and finally vote using this information. Maybe this will happen in the future. But what could happen right now is for Europe to start using indicators differently. We could call on governments, enterprises, associations and citizens to contribute to Europe 2020 in a new way, using indicators like never before to mobilise public opinion to push decision makers in the right direction. A European communication strategy based on statistical indicators could reach, for example, young generations using language they understand, including new visualization and interactive techniques, to build knowledge of where Europe and individual countries stand now, of where they want to go and whether they are getting there.

Because of its importance, statistics have to be produced and disseminated according to professional and scientific criteria, free from political interferences. The European Statistical System, which comprises Eurostat and national statistical offices, has to be strengthened both financially and institutionally. The "Greek crisis" has demonstrated the risk that the weakness of a single statistical institute can be for the entire Union. Therefore, additional measures have to be taken to strengthen the System. In the short term, these measures can be developed within the current legal framework. But in the medium term, it will be necessary to change the current status of Eurostat and of national statistical offices, turning the European Statistical System into a new European System of Statistical Institutes, like the European System of Central Banks, whose powers and independence should be similar to those currently enjoyed by the European Central Bank and national banks. Only in this way can we be sure that the "Greek case" will not be repeated and the trust in statistical indicators will be the highest possible, as it should be.

Statistical indicators are relevant only if they increase knowledge and contribute to actions. In this sense, they can play a key role in political processes, especially in democratic societies. On the other hand, the production of statistical indicators must be done in such a way that their reliability and trustworthiness is recognised by all components of society. This may require institutional changes that should be put on the agenda of future developments of the European Union. Turning indicators into action is possible – and it is necessary now to ensure a better life for current and future generations.

1. Ann Mettler, *Innovating Indicators: Choosing the Right Targets for Europe 2020* (Brussels: The Lisbon Council, 2009).

Innovation and Entrepreneurship: Twin Pillars of Future Success

By Martin Schuurmans

Dr. Martin Schuurmans is chairman of the European Institute of Innovation and Technology (EIT).

Current European innovation efforts are insufficient if Europe wishes to maintain a key role on the global economic stage. As Europeans, we have not been able to compete effectively with the United States and Japan, and countries such as China, Brazil, India and Russia are catching up fast. This is not earth shattering – we have heard this before. What is shocking is that we have analysed and discussed this development to great lengths, but have yet to take the concrete actions necessary to reverse these trends.

Measures are being put into place to address this. Europe 2020 and the recent communication on Innovation Union in particular are steps in the right direction.[1] What we at the European Institute of Innovation and Technology (EIT) and the Directorate-General for Education and Culture at the European Commission are trying to achieve with the EIT is contributing, however humbly, to the re-energising of Europe's innovation efforts. However, unless more people recognise innovation as the key goal of research, education and industry with entrepreneurship in the driver's seat, Europe will continue to stall.

Few can argue with the fact that Europe is very good at science. Taking the medical field as an example, we see that half of the Nobel laureates originate from Europe.[2] So why do so many of the global players in the pharmaceutical arena originate from the US?[3] In reality, Europe only invests about one-sixth of what the US spends on supporting the growth of SME's beyond, say, €5 million turnover.[4] Supporting entrepreneurship does not end after a company has been set up. Resources need to be made available for successful entrepreneurs to take their enterprise to the next level. Europe has a significant gap in funding for further growth of small- and medium-sized companies.

Despite the ambition of the original Lisbon Strategy, agreed in 2000, to set a research and development target of 3% in

> 'Unless everyone starts to recognise innovation as the encompassing factor for research, education and industry with entrepreneurship in the driver's seat, Europe will continue to stall.'

Europe, R&D spending was still at 2.01% of GDP in 2009 in the European Union as a whole. This compares with 2.77% (2008) in the US, 3.6% for Sweden, 2.8% for Germany and 2.2% for France.[5] In comparison, China invested 1.7% of its gross domestic product on R&D in 2009 and aimed to invest 2% by the end of 2010.[6] The continued emphasis in the EU on the 3% Lisbon target is very much supported by the EIT. While it is true that more spending will not automatically lead to more innovation, Europe is simply missing the boat when it comes to the foundation of new companies based on game-shifting technologies. Moreover, the product and services resulting from EU industry R&D, despite the best intentions, oftentimes do not reach the market because they lack the right mix or the right timing for the customer. Few new European companies play a role in the year-upon-year renewal of the Fortune Global 500 list of the world's largest companies.[7]

Entrepreneurship (combined with higher education) and better understanding of customers, markets and sales channels are the key drivers of innovation. Recently, US President Barack Obama appealed to his country to "out-innovate" and "out-educate" the world (first and foremost China) in order to restore economic prosperity and create jobs "to make America the best place on Earth to do business."[8]

Put simply, Europe needs to embrace entrepreneurship and education for entrepreneurship as well as the flexibility of an environment conducive to entrepreneurship. However, we live on a continent where failure is often shameful and risk is preferably avoided. Thus, we primarily educate our young people for employment and safe retirement rather than to become an employer and a risk taker building new companies.

Like the United States, Europe needs to focus on out-educating its youngsters to empower them with a different set of "know how and why" skills and attitudes (rather than knowledge only) and should for example integrate engineering and entrepreneurship education. Successful entrepreneurs need to be offered the right incentives (from mentoring to pre-seed or venture capital to growth capital) to enable innovation to thrive; in short to "out-innovate" their competitors, as our friends across the Atlantic have vowed to do.

We often ask ourselves why our most talented students and researchers decide to follow their dreams in the United States. The answer is simple: these young students and researchers are attracted by an environment which encourages and pushes them to succeed – not one that stifles them in rules and control limiting their flexibility to win over innovation opportunities.

The clock is ticking. Without further concrete positive action, it is likely that by 2020 our children and grandchildren will be growing up in a "me-too economy," with less wealth and limited hope of catching up with the true global economic leaders in the USA, China and (maybe) India.

To bring Europe closer to the "smart, sustainable and inclusive growth" set forth in the Europe 2020 programme, I propose the following three-point programme:

- Put entrepreneurship at the heart of higher education. People are at the heart of any social and economic transformation. So the EU should transform the higher education landscape into one that supports and encourages the creation, production, dissemination and communication of new ideas. Make it a system that fosters entrepreneurial mindsets so that entrepreneurs are able to harvest the fruits of their education. The EIT aims to do just that with our three Knowledge and Innovation Communities (KICs) and their partners. Our intent is to develop EIT-labelled degrees as a benchmark for this process on a wider European scale. And why not create an entrepreneurship "passport" for students (graduates, masters and PhDs) who complete an entrepreneurial education fulfilling certain excellence criteria?
- Put entrepreneurship at the heart of all future EU funding mechanisms as an enabling tool. Entrepreneurship should play a key role in all European policy programmes. Moreover, the EU must ensure greater coherence and complementarity between different sources of funding available for entrepreneurship under the various EU programmes and in different geographical environments in Europe. Well-trained people need good tools. Europe is doing a commendable job on pre-seed money, but the EU should do more to set aside and make available significant sums of money to address the funding gap for small- and medium-sized companies to grow beyond €5 million turnover. Maybe a passport or EIT label can help here too.
- Simplify EU programmes and instruments to achieve flexibility in support of entrepreneurship. At the EU level, we need less complex rules and greater trust to ensure greater flexibility in support of entrepreneurship and innovation. The harmonisation of rules and tools that is currently being discussed in the EU is a form of simplification that can be at odds with the flexibility needed for innovation. The EIT is testing the waters on simplification towards flexibility in several respects. The EIT is moving towards becoming an engaged investor rather than a grant giver, has three KICs led by a CEO and has started to work with fewer rules as enabled by its derogations from the EU Financial Regulation. Although this is a good starting point, there is a need to go further. After all, from the EIT conception in the European institutions to the designation of the first innovation communities took four years; in that same period Facebook and Twitter emerged! Europe should understand that the key principle in fostering entrepreneurship and innovation is first and foremost flexibility.

European competitiveness would only benefit from innovation driven more strongly by entrepreneurship through better entrepreneurship education; embedded, properly funded and incentivized entrepreneurship in all European programmes and simplification of rules and tools towards flexibility in support of entrepreneurship. The time to act is now.

1. For more on the Europe 2020 strategy and the Innovation Union flagship, see European Commission, *Europe 2020: A European Strategy for Smart, Sustainable and Inclusive Growth* (Luxembourg: European Commission, 2010); and European Commission, *Europe 2020 Flagship Initiative: Innovation Union* (Brussels: European Commission, 2010).
2. "All Nobel Prizes in Physiology or Medicine," *Nobelprize.org* 22 February 2011.
3. Patrick Clinton and Mark Mozeson, "The Pharm Exec 50," *Pharmaceutical Executive Magazine* May 2010.
4. Nick Clayton, "U.S. Capital Gets Europe's Tech Stars Up and Running," *The Wall Street Journal* 08 December 2010.
5. Eurostat, "Gross Domestic Expenditure on R&D (GERD)," *http://epp.eurostat.ec.europa.eu*.
6. "China Spends 1.7% of GDP on R&D: Survey," *ChinaDaily.com* 23 November 2010.
7. "The Fortune Global 500," *CNNMoney.com* 26 July 2010.
8. Barack Obama, *State of the Union Address* (Washington D.C: White House, 2011).

Structural Reform:
Key Steps on the Road to Recovery

By Alessandro Leipold

Alessandro Leipold is chief economic adviser to the Lisbon Council. He formerly served as deputy director and acting director of the European Department at the International Monetary Fund.

European leaders meet this Spring at a critical juncture in the European Union's renewed effort at enhancing economic policy coordination and improving governance in response to the financial crisis. Assembling to debate and discuss European reform as they do each Spring, they come together halfway through the first European Semester of Policy Coordination, a key component of this effort. By their own account, the Semester is designed to "provide a European input to national policy decisions, leading to more effective ex-ante policy co-ordination. This also applies to the structural reforms and the growth-enhancing elements of the Europe 2020 strategy."[1]

The first formal step foreseen under the European Semester has already been taken: in early January 2011, the Commission presented its first Annual Growth Survey, a new flagship publication intended to chart the direction for Europe over the coming year. The Survey identified "10 priority actions… anchored in the Europe 2020 strategy," which was itself launched just one year ago and intended as a break from the lacklustre performance of its predecessor, the Lisbon Strategy.[2] Going forward, the Spring 2011 European Council is due to provide guidance to Member States as they finalise their National Reform Programmes (NRPs), which are focused on structural reform as well as on convergence and stability programmes in the fiscal area. In April, Member States are to present their finalised programmes, which will then form the basis for specific policy guidance in the summer, ahead of formal budget adoption in Member States. By then, it is also planned that legislation will have been agreed with the European Parliament to implement the strengthened surveillance over macroeconomic imbalances and divergences in competitiveness foreseen in the report of the Task Force, headed by European Council President Herman Van Rompuy and endorsed by the October 2010 European Council.[3]

'A growth-enhancing structural reform effort has become even more critical in the wake of the crisis and its legacy of high unemployment and depressed potential output.'

The reader will hopefully forgive this bureaucratic opening. Its intention is twofold: first, to highlight that the EU already has – to use terminology currently in vogue – a "competiveness pact" or "grand bargain" agreed by all 27 Member States: it is the Europe 2020 Strategy, complemented by the new macroeconomic surveillance procedures currently being finalised. For the coming year, this broad strategy has been narrowed down in the Commission's Annual Growth Survey into 10 priority actions, endorsed by the Economic and Financial Affairs Council a month ago. The primary concern now must be to give these actions teeth and see to their full implementation. While euro area members may wish to be more specific and ambitious, given the requirements of monetary union, it is neither helpful nor constructive to super-impose new objectives in areas where agreed priorities, the fruit of lengthy deliberations, already exist. Indeed, the risk is that these new initiatives will distract attention from the established priorities, devalue the process, dissipate the consensus achieved, and generate new divisions: the aggrieved reactions to the proposed Franco-German pact in February bear testament to this risk. Nor is it efficient to periodically entrust President Van Rompuy with new *ad hoc* tasks, distracting from his original remit – namely, implementation of the Europe 2020 Strategy.

Second, the listing above also illustrates how removed the process is from national policy-making. It remains, as argued in a Lisbon Council e-brief last year, essentially a "Brussels-talking-to-Brussels" exercise, divorced from civil society and unheeded at the national level.[4] As such, there is little ground to expect it to fare better than its ill-fated predecessor, the so-called Broad Economic Policy Guidelines, widely judged a failure. The process falls well short of that advised in the Europe 2020 Integrated Guidelines where, in order to enhance the impact on national policy-making, it is recommended that the strategy "be implemented in partnership with all national, regional and local authorities, closely associating parliaments, as well as social partners and representatives of civil society, who shall contribute to the elaboration of national reform programmes, to their implementation and to the overall communication on the strategy."[5] In the absence of such broad ownership, NRPs will remain, in essence, documents prepared at the behest of Brussels, destined to a restricted readership, unknown in national capitals, and inconsequential for domestic legislating. Six lessons follow from this:

- First, European leaders should concentrate on securing the success of the programmes and procedures in place and avoid, so early into the process, cutting across these with new, and largely improvised, initiatives;

- Second, leaders should enhance national ownership by ensuring a genuine domestic debate on NRPs and involvement of civil society and parliaments in setting the structural reform priorities for the coming year; and
- Third, leaders should focus reform priorities on at most 3-4 main actionable steps per year, remaining within a scope that is realistic and whose delivery is easily checked.

The last point of course begs the questions: what are the most advisable actionable steps to enhance growth prospects on a lasting basis? What, indeed, are the structural reform priorities at the current juncture? In responding to this question, one must of course pay heed to the first recommendation above, and ensure that the identified priorities are well-anchored in the already agreed initiatives, avoiding untested proposals and confusing super-impositions. And one should be guided by experience: this has clearly demonstrated that common action under Community-level initiatives vested with clear powers (e.g., the Single Market Programme) have been much more successful than soft coordination methods based essentially on peer pressure (e.g., the Lisbon Strategy). Which leads to three more recommendations:

- Fourth, fully mobilise the only readily available Community-level growth engines provided by existing centralized policies – by, first and foremost, expanding the European Single Market (putting into effect the Monti Report) and speeding implementation of the Services Directive. The EU's Single Market remains the most powerful motor of economic growth and integration. Sizeable benefits could be reaped by rapidly transposing the recommendations in Prof. Monti's report on the subject – a seminal study unfortunately overshadowed by the exigencies of crisis response.[6] In particular, with services constituting two-thirds of the EU economy, but remaining plagued by corporatist protections (notably in the professions, retail distribution, transport, and network industries), the effects of liberalisation could be far-reaching. But excessive use is being made of available margins under the Services Directive, running counter to, if not its letter, certainly its spirit; and
- Fifth, to the extent that new initiatives are undertaken – on which main countries such as Germany and France are willing to spend their political capital by providing the impetus[7]– energies should be directed at vesting more reform authority at the central level (at the very least, at the euro area level). Building on the relative success of the "Single Market" initiative, this effort could usefully focus on a "Single Jobs Market" initiative, aimed at achieving a truly integrated labour market, by jointly emulating best practices in key areas and eliminating obstacles to labour mobility within Europe (via, for example, full mutual recognition of professional qualifications and diplomas, the portability of pension rights and the dismantling of national barriers to labour-market entry).[8]

The five recommendations above still leave open the specific steps that each individual Member State should take at the current juncture, and the best guidance that the European Council could provide for the finalisation of the NRPs. Starting positions obviously differ appreciably across countries, and each thus exhibits different roadblocks to growth; these have been well documented in innumerable studies, perhaps most fully by the Commission in a comprehensive July 2010 survey.[9] Such studies show that, while the specifics of remedial measures thus inevitably vary across countries, with the details going beyond the scope of this essay, all countries exhibit similar broad categories of growth bottlenecks. The Commission's Annual Growth Survey's priority actions identify these categories, and the final recommendation, directed to individual Member States, would be as follows:

- Sixth, all Member States should be expected to formally commit to at least 3-4 actionable reforms chosen à-la-carte – according to their importance in unblocking domestic growth and to their national feasibility – from the specific examples provided under the main structural headings of the Annual Growth Survey's priorities, including (a) making work more attractive; (b) reforming pensions systems; (c) getting the unemployed back to work; (d) balancing security and flexibility; (e) tapping the potential of the Single Market; (f) attracting private capital to finance growth; and (g) creating cost-effective access to energy.

A growth-enhancing structural reform has become even more critical in the wake of the financial crisis and its legacy of high unemployment and depressed potential output. To sum up, this effort should focus on implementing current initiatives, notably the Europe 2020 Strategy and the new macroeconomic surveillance procedures; enhance national ownership of reform efforts; fully tap the growth powerhouse provided by already centralised programmes (in particular advancing the Single Market by transposing the Monti Report and speeding implementation of the Services Directive); vest greater reform authority at the central level (aiming ideally at a "Single Jobs Market"); and require Member States to identify 3-4 annual priorities chosen from a common menu. Taken together, such steps would serve to give the EU's structural reform effort much-needed renewed impetus as part of a post-crisis Action Plan, whose main planks are laid out in the other essays of this publication. It is along these lines that scarce political capital is best spent.

1. European Commission, "Enhancing Economic Policy Coordination for Stability, Growth and Jobs: Tools for Stronger EU Economic Governance," *Communication from the Commission* (Brussels, 30/06/2010, COM(2010) 367 final).
2. European Commission, "Annual Growth Survey: Advancing the EU's Comprehensive Response to the Crisis," *Communication from the Commission* (Brussels, 12/01/2011, COM(2011) 11 final).
3. This would include regular assessments and alert mechanisms. Once an alert was triggered, the Commission would make country-specific recommendations (focused largely on structural reforms), possibly issue an early warning, and – in particularly serious cases – recommend placing the Member State in an "excessive imbalances position," triggering stricter (more intrusive) surveillance. See European Commission, *Proposal for a Regulation of the European Parliament and of the Council on the Prevention and Correction of Macroeconomic Imbalances* (Brussels, September 2010, COM(2010) 527 final).
4. Alessandro Leipold, *Good Governance for the Euro Area: Proposals for Economic Stability* (Brussels: Lisbon Council e-brief 08/2010).
5. European Commission, *Brochure on Europe 2020 – Integrated Guidelines for the Economic and Employment Policies of the Member States* (Brussels: European Commission, 2010).
6. Mario Monti, *A New Strategy for the Single Market: Report to the President of the European Commission* (Brussels: European Commission, 2010).
7. Here one must recognize that, despite other countries' sensitivities, Franco-German understandings have often been key to providing the impetus to broader political agreements and to laying the blocks of EU construction.
8. For an elaboration of this proposal, as well as a comprehensive set of recommendations, both at the euro area and country level, see Céline Allard and Luc Everaert, *Lifting Euro Area Growth: Priorities for Structural Reforms and Governance*, IMF Staff Position Note SPN/10/19 (Washington DC: IMF, 2010).
9. European Commission, *Macro Structural Bottlenecks to Growth in EU Member States*, Occasional Papers 6 (Brussels: European Commission, 2010).

Towards a 'Circular' Society:
Building an Eco-Majority for Change

By Harry Verhaar

Harry Verhaar is senior director for energy and climate change at Philips and co-chair of the Eco-Innovation Network at the Lisbon Council.

A few years ago, people still knew very little about climate change or sustainable development. Energy was cheap, raw materials were abundant, and economic growth seemed destined to spiral ever upwards. Since then, we have made a hard landing and are confronted in virtually every aspect of life with a complex, inter-related, three-legged crisis: an economic downturn, a drastic rise in the cost of energy and global climate change.

Today, as we tackle the triple challenge of dwindling global resources (energy, raw materials, water and food), sustainability and climate change, the direction we need to go is crystal clear, but the momentum is just too weak. We are simply not getting to the solutions quickly enough.

When it comes to the mind-set needed to build a low-carbon economy, society can be divided into three broad categories. First there are the "eco-innovators" who actively seek action, but are in a minority. At the other end of the spectrum are what we call the "eco-laggards," who do not recognise, or even refute, the need for action; this group is also in a minority. And third, in the middle, we have the vast majority of society: people who are to some extent "eco-conscious" and agree that action is needed, but who may need a helping hand to commit their support. Our task, then, is to win the hearts and minds of this "eco-majority" and power-up the momentum for change.

In creating momentum for change, it is imperative to understand the core of the issue at hand. Over the past decades, we have created a society that is optimised towards lowest initial cost. Our behaviour has become price-tag focused; most of our decision-making processes (e.g. public tendering) as well as the way we (e.g. consumers, media, politicians, businesses) make our judgments are based primarily on obtaining the lowest initial cost and receiving the fastest instant gratification.

> 'As we tackle the challenges of sustainability and climate change, the direction we need is crystal clear, but the momentum is just too weak.'

This "lowest initial cost" mentality means we are consistently pushing the operational economic and ecological bill into the future. But we already know that the next generation will not be able to pay this bill, let alone ourselves today. In fact, we are the only species in nature that still lives in a fundamentally *linear* society (with GDP as the key indicator) that extracts, consumes and emits resources (energy, water, materials, food), and actually still in some places considers the amount of waste we produce as a sign of prosperity. So we need to move from a linear to a *circular* society (with quality of life as the key indicator) where an effective use and re-use of resources – starting with energy – creates a competitive economy centered on the health and well-being of our citizens.

Our second challenge in winning the hearts and minds of the eco-conscious majority is to shift emphasis to the social benefits of sustainability programmes and activities. We all know the economic arguments about energy-efficient products and processes. Lighting, for example, represents 14% of Europe's electricity consumption. Significant savings are possible – on average 40% – by switching to energy-efficient lighting solutions. In fact, if this 'switch' is completed before 2020, these savings on a European level can amount to €28 billion in reduced electricity cost, 98 million tonnes of CO2, or the equivalent of 141 power plants (in itself representing a €300 billion savings in reduced need for power infrastructure). Yet these arguments alone have not propelled sustained action. We must now focus on the social benefits of sustainability drivers, rather than the drivers themselves, to ensure emotional resonance and so secure commitment.

Our third challenge is to develop and apply a new, more emotionally appealing lexicon that highlights the benefits of making positive resource-efficiency choices. How many ordinary people would be inclined to send their children to a "low-carbon school?" It sounds quite off-putting. Or a "green" school – it sounds better, but could carry a political connotation for many parents. At Philips, we call schools with energy-efficient systems "bright schools," a much more appealing designation, with its allusion to better light, better learning and so brighter children. The narrative and language we use is going to be a key in changing behaviour and having people join in on the journey. And there are other benefits as well. Our dedicated classroom lighting – which allows teachers to adjust both the brightness and warmth of the light to suit the activity at hand – has been proven to promote learning by boosting children's concentration, motivation and behaviour and supporting their general feeling of well-being.

When we answer these challenges – and win the emotional buy-in of the public at large – it will translate to changed voting and buying behaviour of individuals. It will also provide much needed impetus for cooperation between the business community and key public stakeholders, who in new public-private partnerships can tackle the enormous task of building the low-carbon economy and transforming our linear society into a circular and sustainable one.

In concrete terms, we need three types of measures to drive this process forward:

- First, adopt dynamic energy performance standards, raising the bar as technologies progress to phase out old inefficient products, and combine this with innovative ways to make energy consumption visible and transparent (e.g. through increased use of smart grids, web applications and social media);
- Second, legislate to encourage the renovation of all existing building stock and other city infrastructure with energy and resource-efficient solutions and approaches. An ambitious commitment to 3% annual energy-efficiency improvement (compared to the current commitment of 1%) would reduce Europe's need to invest in zero-carbon energy infrastructure (renewable energy; nuclear; carbon capture and storage) up to 2050 by a factor of three, thus dramatically relieving future European budget constraints.
- Third, embrace a novel approach to financing solutions, encouraging investors to look more closely at the upfront life-cycle impact of decisions. An example would be a "green budgeting" mechanism that would integrate capital and operational expenditure, requiring operational expenses (dominated by rising energy costs) to be considered up front.

All of the above measures are not "just" about saving the planet, but much more about creating a prosperous future for Europe, where people have good jobs and enjoy the best possible quality of life.

Mobilising Europe's Collective Intelligence for Social Innovation

By Geoff Mulgan

Geoff Mulgan is chief executive of the Young Foundation. From 1997 to 2004, he served in several UK government roles, including director of the prime minister's strategy unit and director of policy at 10 Downing Street under Prime Minister Tony Blair. He is a member of the Lisbon Council's Board of Advisers.

The challenges Europe faces are well known. Today, we have both the virtues and vices of maturity. The virtues include relative stability, strong institutions and a great deal of accumulated knowledge and wisdom. The vices include rising dependency ratios, inflexible institutions and a longstanding challenge of generating new knowledge, new industries and new jobs.

To turn our vices into virtues, Europe has no option but to evolve. That sounds easy. But evolution never is, and it's particularly difficult for settled societies and incumbent institutions. Evolution in nature involves mutation, selection and replication. But deliberate mutation, the task of creatively multiplying options and possibilities, is particularly hard for bureaucracies. Selection can be even harder, especially for politically accountable institutions, since it involves admitting that some things have failed. Harder still is the task of growing and replicating the mutations and new ideas that work, since that means shutting down and decommissioning the institutions and programmes that don't work well enough.

Much of this is reasonably well understood in business, where thanks to the influence of Joseph Schumpeter and others, it's recognised that Europe needs more entrepreneurship, more investment in new ideas, more open markets and more sophisticated strategies for growth. But Europe's ability to mobilise its collective intelligence to create wealth remains uneven at best. In recent years, Europe has given the world everything from Skype to monoclonal antibodies, the worldwide web to zero-carbon towns. But it's often been negligent in making the most of its knowledge and its capabilities. Two out of three of Europe's best young researchers choose to leave, often to the US. Too many of our research institutions are rigid, hierarchical and poor at making creative use of young talent. And too many of our 4000 or so universities and higher education institutions have been slow to see the connections between disciplines which are where some of the most important innovation is happening.

'Systematic innovation matters as much in society as it does in the economy.'

The challenge is even greater in relation to social and public innovation, where there is a vast gap between the creative fertility of much of society and the relative stagnation of many institutions. Part of the reason is that in earlier decades social and economic policies were thought of as separate. The economic challenge was to generate more products and firms – the higher the technology, the better. The social challenge was to use the proceeds of growth to finance an evolving social model with welfare, healthcare and education. Entrepreneurship mattered for the first task, but not the second. This was, roughly, the story of the Lisbon Agenda. Now, however, we know that the economic and social are much more interwoven than this implied, and that systematic innovation matters as much in society as it does in the economy. The largest sectors of the economy, and some of the ones most likely to grow, are ones with a strongly social content. Health accounts for between 7 and 13% of GDP, and 17% in the US where it's forecast to grow to as much as 48% by the later decades of the century.[1] Education is typically around 6% of GDP. Eldercare and childcare are growing fast, as are the many industries associated with the environment. All are bigger than cars, computers, ships or agriculture. Not surprisingly these sectors are increasingly coming to be seen not just as cost burdens to be funded, but also as sources of comparative advantage, trading income and growth.

Every survey of the future shape of the economy reinforces the point. Manufacturing and business services will continue to be hugely important, and Europe is right to be concerned about its weaknesses. But they are only part of the picture. A recent survey on new sources of growth from Accenture identified the "silver economy," the new markets associated with ageing, as the most important growth area; next came the many innovations around energy, from electric cars to smart grids, all of which depend on changing policies and changing patterns of behaviour as well as new technologies.[2]

This shift in thinking about the economy is being matched by a change in how we think about the balance between sectors. The twentieth century political debate was dominated by a to and fro between the private sector and the public sector. But for several decades, the third sector of civil society has been recognised as a vital complement to business and the state, and its size and confidence has been growing. Now almost every part of Europe has a thriving ecology of social enterprises, coops, mutuals, charities and community organisations, some reanimated by the myriad ways in which the Internet can be used for citizen organisation. Once they were seen as marginal backwaters, yet they're playing leading roles in key growth sectors like eldercare or neighbourhood energy and are set to play an important part in shaping Europe's future.

Governments, too, are having to adjust their thinking. Once government was mainly thought of as an administrative hierarchy, taking in political instructions at the top, and pushing out laws, directives and programmes at the bottom. Now we realise that the public sector just as much as the private sector needs institutionalized innovation if it's not to stagnate, with better ways to create new ideas, better ways to test them and better ways to spread them. Current GDP statistics obscure this point, in that the public sector's contribution to growth is measured by how much they spend, rather than the value of what they achieve. But increasingly governments want to focus more sharply on how to boost public sector productivity, doing more for less, automating processes where possible, raising quality and doing better in preventing costly problems.

Together these shifts are forcing a change in how we think about innovation. In the last quarter of the twentieth century, every ambitious nation tried to expand investment in R&D. Silicon Valley was the model that inspired Taiwan, Israel, Finland and Singapore to pump money into universities, venture capital and spin outs, even if each ended up with radically different models. Now any nation that aspires to the first rank has to invest 3-4% of GDP into future science and technology.

But this is no longer enough. Instead the changing shape of the economy, the rising importance of civil society, and the changing views of the public sector require a revolution in how innovation is understood and supported. As the Innovation Union strategy recognised, for Europe to thrive innovation has to be cultivated in every field; it's no longer just the prerogative of big laboratories, universities or venture capital funds, but matters as much for public services, community groups and citizens themselves. Evolution matters as much for schools, hospitals and prisons as it does for factories and IT systems.

We start with many strengths. Europe is rich in institutions concerned with civil society and has developed new banks like Banca Prossima and Banca Etica in Italy, investment funds like Sitra and Tekes in Finland, as well as impressive foundations like Gulbenkian in Portugal and Bertelsmann in Germany. But our institutions for social and public innovation remain far weaker than their equivalents in traditional research and development, with few mature sources of finance and skill.

So what is to be done? And what could be achieved? By 2020, we need our continent to be full of creative new approaches to issues like disability, drugs, crime and transport. We need Europe to become good at recognising successful innovations and even better at adopting them, and we want the rest of the world to see Europe as a continent where the future is being created – from low-carbon communities to networks for self-managed healthcare. To achieve this goal we need much more systematic and energetic action to accelerate evolution:

First, every government should earmark at least 1% of every public budget for innovation – a modest investment in the future that would quickly pay for itself. New funds should be invested in funding individuals as well as groups and organisations, and backing them to take their ideas from sparks into investible projects and programmes. That means a new generation of innovation funds and challenge prizes to mobilise citizens' brainpower to develop better answers to helping older people stay active, to cut crime or shrink carbon footprints. It also means R&D programmes that are opened up to civil society, and that place as much emphasis on new service, business or organisational models as they do on new hardware. And it requires investment in innovation skills – so that Europe's innovators are familiar with the best methods in design, incubation and finance.

Second, Europe needs to do better at selecting what really works. That means a clear commitment to evidence, with transparent processes to judge what works and what is cost effective, drawing on models like the Cochrane Collaboration and the National Institute for Clinical Excellence (which publicly rules on what works and what's cost effective in health) as well as the work of bodies like the OECD. In every area of public service and public policy, we need accessible, useable guides to what works and what's cost effective, so as to put pressure on public sectors to decommission obsolete projects and programmes, and scale up alternatives that are better placed to deliver value for money. In the private sector, market forces provide an unambiguous measure of whether innovations succeed or fail: we need comparable measures for public and social innovation.

Third, Europe needs to incentivize effective innovation. Part of the answer is to mobilise new sources of capital to finance social investment banks, and social venture funds providing a mix of grants, loans and equities for high impact new ventures. But just as important will be new funding models that reward successful innovation and contribute to growth. Structural funds could be reshaped so that they incentivize results, drawing on the idea of "social impact bonds."[3] Instead of funding programmes or activities, funds would be tied to deals between the European Commission, governments and regions, with significant tranches of funding only released once measurable outcomes, such as more jobs for young people, have been achieved. Funding mechanisms of this kind would encourage greater innovation and more take-up of proven models from elsewhere.

Linking all of these points is the need for a change of perspective. Economic and industrial policy needs to become more attuned to social needs, priorities and opportunities. But conversely social policy needs to become more attuned to questions of productivity and innovation. The strong lead from José Manuel Barroso, president of the European Commission, and Maire Geoghegan-Quinn, commissioner for research and innovation, is already galvanising action. The challenge now is to embed this new thinking into Europe's institutions and into the strategies of national governments, regions and cities. If we get this right, and learn how to mobilise Europe's collective intelligence, we may even turn some of our problems into opportunities.

1. Congressional Budget Office (CB0), *The Long-Term Outlook for Health Care Spending* (Washington D.C.: US Congress, 2007).
2. Accenture, *New Waves of Growth: Unlocking Opportunity in the Multi-Polar World* (London: Accenture, 2011).
3. Geoff Mulgan, Neil Reeder, Mhairi Aylott and Luke Bo'sher, *Social Impact Investment: The Opportunity and Challenge of Social Impact Bonds* (London: The Young Foundation, November 2010).

Unleashing Europe's Digital Economy: Platform for 21st Century Success

By Žiga Turk

Žiga Turk is professor and chair in construction informatics at the University of Ljubljana in Slovenia. From 2008 to 2010, he was secretary general of the European Union's Reflection Group on the Future of Europe, headed by former Spanish Prime Minister Felipe González. He is a member of the Lisbon Council's Board of Advisers.

A transition to a different kind of economy is underway. You can call it the "information," "knowledge" or even the "meaning" economy. The transition goes well beyond the boundaries of normal economic activity, reaching out into the fabric of society itself. Increasingly people are spending money on information-based goods. And they are working more in information-based jobs, where they create and handle information as opposed to the old "material jobs" where they handled mostly material things. Moreover, the material products and services people make today are themselves increasingly knowledge and information intensive. A substantial proportion of the product's value is not related any more to labour, energy or the material used to produce them.

Ideas – information, knowledge and meaning – are being created with the assistance of information and communication technologies (ICT) that have been digitised. The digital economy is not just about digital products (software, content, media) or digital services (communication, data transfer, storage). Rather, digital technology has become a key tool to create, manage and communicate "ideas" related to all products and services to every part of society. The issue is not "digital economy" versus "industrial economy." It is about figuring out how the digital economy will transform industries and societies, improve productivity and increase added value.

Europe has had its share of leading ICT innovations. The World Wide Web was invented in Europe's CERN. A Finn developed Linux, disrupting the operating system market and bringing the open source paradigm to a whole new level. A Swede and a Dane invented Skype, shaking up telephony. Nokia, Ericsson and Siemens dominated the early days of the mobile telephony business. Fraunhofer Institute invented the MP3 codec that changed the music industry. Last and least, the author of this essay invented a search engine for freeware and shareware in 1990s.

'The issue is not "digital economy" versus "industrial economy." It is about figuring out how the digital economy will transform industries and societies, improve productivity and increase added value.'

But Europe too often failed to translate this technical leadership into businesses and jobs. The first decent commercial Web browser was created by Netscape in the US, which went on to dominate Internet services and content, starting with Yahoo!, followed by Google and Facebook. Linux powered the servers of Silicon Valley start-ups that evolved into market leaders. Skype was sold to eBay. The smartphone market is now dominated by North Americans – Apple, RIM and Google. The only company making real money from selling music in the originally "European" MP3 format is Apple with iTunes. And it was an American company that commercialised my search engine and grew it into http://www.download.com. Today, Europe does not have a single company among the top 20 in BusinessWeek's Tech 100 list.[1]

Europe's failure to be competitive in the ICT sector is just a symptom. The causes are deeper: a generally uncompetitive business environment, systemic rigidities, unresponsiveness, fragmented markets, lack of concentration, many non-tariff barriers and underdeveloped financial services. Europe is failing to translate world-class science and technology into growth and jobs. The ICT sector is moving too fast for the way we do business in Europe, for the way our societies are organised, for the way we combine creativity and entrepreneurship. In the new and fast growing ICT sector, our excellent traditions and better starting positions in some industries are unable to obscure the increasingly evident shortcomings of our socio-economic models.

It would be unfortunate if Europe's emerging digital strategy would only treat the symptoms. IT and the Internet have been on the political banners of the EU at least since 1994.[2] ICT and the "knowledge-based economy" were prominently represented in the Lisbon Strategy. The Digital Agenda for Europe is one of seven flagship projects in the Europe 2020 strategy.[3] The wise man's group Project Europe 2030 called for the completion of the single market "to include services, the digital society and other sectors."[4] There is no shortage of visions, such as Future Internet 2020[5] or The Digital World in 2025.[6]

The ICT industry likes being in the limelight like this, and is happy to support various plans and agendas that would give it a priority status in R&D funding or call for investment into the products it sells. But many of these same "national champions" would not, with a similar vigour, support measures that would make competition on the European markets tougher. In Europe, the providers of connectivity have an upper hand when compared to the providers of intelligent services and software that sits on top of that connectivity. With local loop unbundling, we created perfect conditions for local and dumb infrastructure providers, not for global and smart service providers.

Europe knew better in the distant past. During the "dark" Middle Ages, the foundations of European capitalism were laid. Free city states between Rome and the Alps competed (rather than agreed on common economic policy) to see who could create the best business environment. In Sienna, Lucca and later Florence, the first truly European banks such as Gran Tavola dei Bonsignori, Ricciardi and Medici appeared and financed kings and popes, trade and wars. The first universities were founded. Also in the 13th century, the Magna Carta set out to protect the rights of property owners. Hand-copied books of the time included a curse against stealing content.

In other words, in the Middle Ages, Europe was busy laying the foundation of future success. It created the financial services market, knowledge institutions, IPR policy, along with an ethical and legal infrastructure into which the originally Chinese invention of paper and printing was planted. European civilization was the clear winner in the paper communication revolution. But it seems to be a laggard in the Internet communication revolution.

To reverse this trend, we must urgently do the following:

- The European financial sector should be motivated to look for high-risk, high-return opportunities in high-tech. Today, too much capital is interested only in secure, low-risk support of national pension plans or servicing the debt of Industrial Age industry. The whole culture of venture capital in its essential meaning – to venture – is missing.
- The Single Market needs to be deepened and completed, particularly in services. ICT is related to all areas of economy and governance, but is even more related to services than to products. This includes public services such as healthcare and education. In general, a single market for services would create a single market for the digital support of those services. In particular, the EU should ensure that the concept of roaming has nothing to do with national borders. Regulating the price of SMS and mobile voice telephony was popular, but addressed yesterday's issues. By contrast, the policy of adopting flat-rate mobile-data access across Europe would create a market for mobile services, which could have perhaps prevented the sunsets of the Nokias and Ericssons.
- Intellectual property rights systems should have one single goal: to encourage intellectual property creation. Energy should be shifted from legislation that is focusing on how to replicate the IPR regimes for the material and paper paradigm in the digital world towards legislation that would maximize the impact that open innovation and creativity can bring.

But we already know this. As Martin Bangemann wrote 17 years ago in his seminal report: "Actions must be taken at the European level and by member states to strike down entrenched positions which put Europe at a competitive disadvantage: it means fostering an entrepreneurial mentality to enable the emergence of new dynamic sectors of the economy; it means developing a common regulatory approach to bring forth a competitive, Europe-wide market for information services; it does NOT mean more public money, financial assistance, subsidies, dirigisme, or protectionism."

That was clear in 1994, and it demonstrates perhaps the biggest problem of the European digital economy: Much as Europe is unable to translate science and technology results into commercial products, European politics is unable to translate the recommendations of high-level, expert and reflection groups into political action. The problems holding back the European digital economy have little to do with the digital economy itself.

1. Jennifer L. Schenker, "Meet the Tech Pioneers 2011," *BusinessWeek.com* 02 September 2010.
2. European Union, *Bangemann Report, Europe and the Global Information Society* (Brussels: 1994).
3. European Commission, *Communication from the Commission to the European Parliament, the Council, the European Economic and Social Committee and the Committee of the Regions: A Digital Agenda for Europe* (Brussels: European Commission, 2010).
4. Felipe González et al., *Project Europe 2030: Challenges and Opportunities. A Report to the European Council by the Reflection Group on the Future of Europe* (Brussels: May 2010).
5. European Commission, *Future Internet 2020: Visions of an Expert Group* (Brussels: European Commission, 2009).
6. European Internet Foundation, *The Digital World in 2025: Indicators for European Action* (Brussels: European Internet Foundation: 2009).

New Waves of Growth: Releasing the Potential

By Mark Spelman

Mark Spelman is global head of strategy at Accenture and a member of the Lisbon Council's Board of Advisers.

The time has come for European leaders to shift their focus from sovereign-debt management to unleashing new waves of growth. Sorting out the eurozone debt trap with credible structural reforms is necessary. But it is not sufficient. The European Union needs to embrace the Europe 2020 strategy and develop more precise roadmaps for delivering growth this decade. Aspirational targets have their place, but they need to be underpinned by commitments and milestones from both European and national leaders.

There is significant, new, and largely untapped growth opportunities contained in some of the important economic and social trends we see: the ageing population, pressure on natural resources and the convergence of new technologies. Conventional wisdom views ageing as a problem. But the "greying" of the population also represents an opportunity. The number of people over 60 will grow by 17% in the UK and 14% in Germany this decade. By 2020, Germany will have 24.5 million people over 60, of which six million will be over 80. Many industries will benefit from the surge in age-related demand – particularly healthcare, financial services and consumer products. There will be more health diagnostics, self-help programmes and home-based healthcare services. Financial services will adapt to the needs of an ageing population with tailored equity release products and new health insurance plans, while consumer goods will be adapted to the changing physiological condition of older people. Learning and leisure are two other areas with large potential. The provision of tailored education will enable growing numbers of older people to refresh skills and seek new mental stimulation over a longer working life, while the delivery of leisure services such as entertainment, travel and tourism will find growing demand in the "silver economy."

The response to the squeeze in global resources – land, water, energy, food and

'Conventional wisdom views ageing as a problem. The "greying" of the population represents a significant untapped growth opportunity.'

minerals – can also present fertile terrain for growth and new jobs. There is already a strong European focus on green capital goods and infrastructure from photovoltaic systems, wind turbines, carbon capture and storage, smart buildings, remote sensors and meters. However, the opportunity is broader; increased regulation and pricing of carbon will create demand for carbon finance, green investment funds and energy mapping. Growing populations coupled with changing diets and lifestyles will drive demand for food and high value agri-businesses in areas such as processing, handling, packaging, transporting, marketing and distribution of food products. Land degradation, climate change and water scarcity will put a premium on efficient land and water use. The global market for desalination technologies alone is expected to reach approximately €40 billion by 2015.

Technology is central to economic progress, including productivity improvements and the improvements of living standards. The volume of data and the surge in computing processing speeds will continue this decade. Breakthroughs centered on innovations in information and communication such as superfast broadband and cloud computing, materials and nanotechnology, mobility and robotics, mobile and remote sensors as well as genomics and biotechnology all represent a range of growth possibilities.

Ageing, resource constraint and new technologies are three examples of underexploited potential growth sectors. These trends are pervasive – people will live longer, energy and natural resources are already becoming scarcer and technology is marching onwards with more applications and more users. With the right responses from governments and business, these trends can represent strong bets for future growth and job creation. Modeling of the UK and German economies shows that with the right policies, annual GDP growth rates could be on average 0.5-0.7% per annum higher, creating an additional 2.5-3.0 million jobs in each country by 2020. The growth prize is significant not just for Germany and UK, but for the whole of the EU-27.

The opportunity for accelerated growth and job creation could be easily lost because the trends are largely inevitable but the benefits are not. The reason is many European economies lack the supply-side factors that stimulate growth – the right quantity and types of skills, underlying infrastructure, technology standards and innovation systems. There needs to be a stronger linkage between EU and member state growth initiatives. Given that one size clearly does not fit all, countries will have different points of leverage, but the combined effect should be a strong push for higher growth and better execution, at both the European and country level.

For the Member States
Each member state country should complete a growth plan for 2011-2020 focused on growth opportunities, supply side initiatives and exports in a way that goes beyond many of the fiscal measures set out in the European Commission's recent Growth Survey.[1]

- Adopt a strategic view to new growth waves.
  Each country should identify growth waves such as ageing, resource scarcity and technology and define their potential impact on GDP growth and job creation. Governments need to adopt a more strategic view of growth by understanding the investment frameworks, organisations and action steps required over a one-, five- and ten-year horizon. This is not about picking winners, but learning from countries like Indonesia and Columbia to create the engagement, commitment and plans to deliver an acceleration in growth and jobs.
- Improve the supply side.
  To underpin growth, each country needs to develop plans to strengthen skills and innovation in line with the new growth waves.
  a) Skills – widening the net to retain older people in the workforce, encouraging younger people to develop STEM skills and strengthening digital skills;
  b) Innovation – strengthening the links between scientific research and entrepreneurs by deepening the interchanges between academia, research universities, start-up businesses and larger companies both within country and across borders;
  c) Enabling infrastructure – building the technological arteries of the economy for new energy solutions, mobile, connectivity, super fast fibre optics and improved transport links.
- Exports.
  Identifying growth export markets by understanding where countries and regions have comparative advantage. This will involve looking at consumer and infrastructure requirements in:
  a) Established markets within the EU and US
  b) New export markets, revitalising old trading links where appropriate and leveraging the near markets of Eastern Europe, Turkey and the former Soviet Union countries.

The plans should include agreed targets by a cross section of public, private and civil society organisations to accelerate growth by setting interim milestones for one, three, five years with a clear roadmap for how the growth will be delivered.

For the European Union
The European Union should focus on three growth priorities in 2011: Doha, the Single Market and a Growth Summit.

- Doha.
  Freeing up trade and investment through global agreements is one of the best routes to fuel growth. There is less than one year left to agree the drawn out Doha round: the search to close the gaps in the next six months is critical. Pushing for more ministerial face time within the EU and with trade partners is an important step to avoid a bottleneck in negotiations at the end of the calendar year.
- Single Market.
  Deepening and broadening the European single market is vital given the size and scale of intra-EU trade in goods and services. The momentum to improve cross-border procurement, create a single energy market and accelerate the development of a digital single market will have a significant impact on the prospects for EU growth this decade. Moves to improve standards and interoperability will be beneficial. However, the critical issue is speed of implementation and finding the right carrots and sticks to ensure the core features of the single market are implemented.
- Growth Summit.
  Plan for a EU growth summit at the end of 2011 to assess progress on the Europe 2020 strategy, national growth plans and the prospects for Doha. This will provide the context for setting growth priorities and milestones for 2012 and 2013.

The recovery is not complete in Europe and will require more work, but insufficient attention is being paid to internal and external sources of growth. There is significant untapped potential. Now is the time to seize hold of the growth opportunities. Building and expanding on the Europe 2020 strategy must be a critical priority for 2011, if Europe is to break the shackles of relative underperformance.

1. European Commission, *Annual Growth Survey: Advancing the EU's Comprehensive Response to the Crisis* (Brussels: European Commission, 2010).

Entrepreneurship, Here and There: Being the Best We Can Be

By Sören Stamer

Sören Stamer is CEO and founder of Yokudo, a start-up company aimed at connecting artists more closely to their fan base. His previous start-up, CoreMedia, which he sold in 2009, was one of Germany's fastest growing Web services companies. Born in Hamburg, he lives today in Silicon Valley. He is a member of the Board of Directors of the Lisbon Council.

There are moments when you feel invincible, moments of pure elation and tomorrows filled with possibility. Then there are moments when you stumble on hard realities, when unexpected troubles drain your energy and turn your stomach. Despite the numerous hurdles to creating something from nothing, entrepreneurs continue to emerge, willing to tackle the unknown. Their victories and challenges are our own, since the technology they develop through entrepreneurship and innovation will determine our future. As the techno-sage Marshall McLuhan once said, "We shape our tools and thereafter our tools shape us."[1]

As in the past, change will happen in unforeseeable ways, and—given the accelerating rate of innovation in a global, networked society where ideas careen around the world in seconds—the transformation will be even more fundamental than anything we have experienced before. To address this new reality, Europe must change its policies regarding entrepreneurship and innovation.

In the last 20 years, the World Wide Web—one of the greatest European inventions of all time—has given birth to an avalanche of innovations. People around the world share ideas and participate actively in the emerging global information society, with the majority having daily access to mobile communications and the Internet. For the first time in history, they are able to actively participate in a truly global market, a paradigm that is changing the competitive landscape for many industries.

Global social networking and the ubiquity of mobile phones—over 5.3 billion subscribers at last count—are also disrupting the balance of power between central authorities and the people.[2] As a result, start-ups like Facebook and Twitter have become platforms for people not only to poke and follow their friends, but also to build powerful movements for social change as we have seen with the wave of popular revolutions in the Middle East and North Africa.

'Europe must increase its appetite for change and embrace innovation to attract risk-taking entrepreneurs and enable more high-growth start-ups.'

Entrepreneurship and innovation are key forces for economic growth and new employment. In this increasingly networked world, rising complexity and the rapid rate of change will continuously shift the competitive advantage from big, established companies to innovative, agile newcomers.

Given these dynamics, Europe will face intensifying global competition. As global network effects widen the gap between the winners and the rest, the stakes are higher than ever before: Europe's policies for innovation and entrepreneurship will have a profound impact on Europe's future competitiveness.

Europe is well-positioned to capitalize on this rapid innovation cycle. The European Union has created the largest integrated market and the highest standards of living globally, it stands for diversity, peace, stability, fairness and justice, culture and tolerance, with many countries hoping to join the European Union at some point in the future. Europe should build on these strengths and aim to become a beacon of entrepreneurship and innovation in the world.

So how can the Europe 2020 Agenda help?

According to Anders N. Hoffmann, the real policy challenge for the European Union in the field of entrepreneurship is not a lack of start-ups, but a lack of fast growth in start-ups.[3] I agree with this view. European entrepreneurs must deal with Europe-specific barriers if they want to grow fast. Drawing on my own personal experience as a European entrepreneur who recently moved to Silicon Valley to start a new company, I propose three action items to overcome these barriers:

1. Embrace change

When I stumbled upon Joseph Schumpeter's work on entrepreneurship and innovation several years ago, I realised more fully why I had been drawn to being an entrepreneur. Schumpeter noted that the creative destruction resulting from innovation and entrepreneurship is the force that creates sustainable long-term economic growth.[4] His conclusion that radical innovation will lead to a better society captures the essence of what has motivated me to build new companies.

However, Schumpeter's work seems to be interpreted differently in the United States (and especially in Silicon Valley) than in Europe. My impression as an entrepreneur is that Europe tends to optimise existing structures, while Silicon Valley has a greater appetite for radical change. This difference in attitude has consequences for the availability of venture capital, the focus of entrepreneurs, and the social acceptance of failure. "Fail often, fail fast" is the mantra of Silicon Valley. Having tried something and failed is generally perceived as a badge of honor and as good preparation for the next venture, whereas, in Europe, there is still a stigma associated with failure.

This fast-learning culture has become a defining quality of the Silicon Valley ecosystem. It is evident not only in small start-ups, but also in established, market-leading companies. As a result, the collective learning curve of companies in Silicon Valley tends to be significantly higher than of those in Europe. A case in point: Apple's entry into the smart phone market with the iconic iPhone was rewarded with global market dominance (today, after only three years, the iPhone accounts for more than 50% of all profits in the global cell-phone market).[5] Google quickly followed their lead and launched the Android mobile operating system. Again, after just three years, Android became the global market-leader for smartphone software.[6] Nokia, on the other hand, one of Europe's long-standing stars and the dominating mobile phone market leader of the last decade, has not been able to innovate with nearly the same pace and has been heavily punished with declining market share and lost momentum.[7]

Europe must increase its appetite for change and embrace innovation to attract risk-taking entrepreneurs and enable more high-growth start-ups. The Europe 2020 Agenda should promote more angel investment in early stage start-ups and bankruptcy laws that prioritize successful re-starts.

2. Create a single, large and unified market

The sheer size of the unified US market versus Europe is another major difference. While the European market as a whole is larger, it remains fragmented by languages, national structures and local cultures. US start-ups have a significant competitive advantage before they are even out of the gates. While local cultures and languages are rightly here to stay, national regulatory and legal structures should be re-evaluated. Do the disparate copyright regimes, telecoms regulations and privacy standards, for instance, create value for European citizens by being country-specific? Some might be more of a cumbersome legacy than an asset.

At the same time, Europe's diversity can be an advantage for start-ups that want to address a global audience in a localised way. Tailoring offerings to local cultures and business practices is a potential strength of European start-ups. However, legal and structural hurdles can stand in the way and must be addressed in order to increase the chances for fast-growth start-ups to emerge.

The EU should aim high in order to create the best legal framework possible for a global networked society. The Internet brings new challenges for legal systems around the world. Not all existing laws make sense given the reality of the Internet as a global medium, and new aspects need to be regulated for the first time. How are privacy, free press, and freedom of speech to be handled best in a global networked society? The Europe 2020 Agenda should make these questions into top priorities.

3. Establish dense and diverse networks

It has been observed that the rate of innovation is increased when specific geographic areas have a higher density and diversity of people organised around a common industry.[8] Europe should adopt this approach to foster innovation.

San Francisco and the Silicon Valley are full of ambitious people who want to make the oft-mentioned "dent in the universe," and all of them believe they can. In this region, the density of highly networked, like-minded people creates an ecosystem that enables the fastest dissemination of ideas I have experienced thus far. The chance to be a part of this ecosystem attracts entrepreneurs from around the world, further increasing the density and diversity. Over half of all start-ups in Silicon Valley has one or more immigrants as a key founder.[9]

Europe would also benefit from opening up more and attracting global talent through proven lures: high-quality universities (that are more affordable than those in the US), an attractive visa program for entrepreneurs and their families and a fair chance to become a European citizen.

Europe can further increase the effective density and diversity of Europe's citizenry through greater Internet access. To enable an even denser social network and more elaborate idea exchange, the Europe 2020 Agenda should make low-cost, trans-national broadband access to the mobile Internet a top priority.

The Europe 2020 Agenda offers a great opportunity to shape Europe's role in a global, networked society. Promising developments like the recent rise of Berlin as a hotbed for start-ups in the creative space show Europe's potential. Entrepreneurship and innovation will be key drivers of progress and change in the next decade. By taking the three steps outlined above, Europe can and should position itself as a vibrant ecosystem for innovation.

1. Marshall McLuhan, *Understanding Media: The Extensions of Man* (New York: McGraw Hill, 1964).
2. "Global Mobile Statistics 2011," *MobiThinking.com* February 2011.
3. Anders N. Hoffmann, *Promoting Entrepreneurship – What are the Real Policy Challenges for the European Union (EU)?* (Copenhagen: Danish Ministry of Economic and Business Affairs, 2006).
4. Joseph Alois Schumpeter, *Capitalism, Socialism and Democracy* (New York: 1942).
5. "iPhone Market Share: 17.25% of Smartphones, 4.2% of All Phones," *OsXDaily.com* 01 February 2011.
6. Tarmo Virki and Sinead Carew, "Google Topples Nokia from Smartphones Top Spot," *Reuters* 31 January 2011.
7. Stephen Elop, "Full Text: Nokia CEO Stephen Elop's 'Burning Platform' Memo," *The Wall Street Journal* 09 February 2011.
8. Brian Knudsen, Richard Florida, Gary Gates, and Kevin Stolarick, *Urban Density, Creativity, and Innovation* (May 2007).
9. "Skilled, Educated Immigrants Contribute Significantly to U.S. Economy," *ContactoMagazine.com*

Europe and the World:
The External Dimension

By Parag Khanna

Parag Khanna is senior research fellow at New America Foundation and author of *The Second World: Empires and Influence in the New Global Order* and *How to Run the World: Charting a Course to the Next Renaissance.*

Europe has been a systemic anchor of world order since ancient times. It has shaped every major era of history including the Middle Ages, modern inter-state system, colonization and the Cold War. To retain its worldwide significance in the coming decades to 2020 and 2030, Europe will need to ensure that its external strategy is a global one.

The US National Intelligence Council has already conceded Europe's success. Its *Global Trends 2020* report states that "Europe's strength could be in providing a model of global and regional governance to the rising powers….The European Union, rather than NATO, will increasingly become the primary institution for Europe, and the role which Europeans shape for themselves on the world stage is most likely to be projected through it."

If stability and prosperity go hand in hand, then Europe must not lose sight of the long-term drivers of both: widening and deepening. A consistent and collective commitment to both drivers has been and continues to be essential for Europe's long-term success. There are numerous internal scenarios which portray a European stability and prosperity threatened by uneven fiscal fundamentals between the core and periphery, varying ability to integrate immigrants and manage social unrest, and difficulties coping with the challenge of ageing populations. But European leaders cannot let internal economic obstacles overwhelm the imperative of building a long-term basis for growth and influence on the world stage.

Even in a period of slow economic growth and delayed structural reforms, externally oriented policies are key to maintaining momentum for the EU as a whole. For example, European companies are currently successfully signing large long-term engineering and infrastructure contracts in the fast-growing economies of the Persian Gulf region and Asia. This generates high-

'Calculations of global power frequently hinge on demographic size and economic growth.'

skilled jobs on the continent as well as sizeable profits. Aggressive commercial expansion is therefore fundamental to a strong Europe.

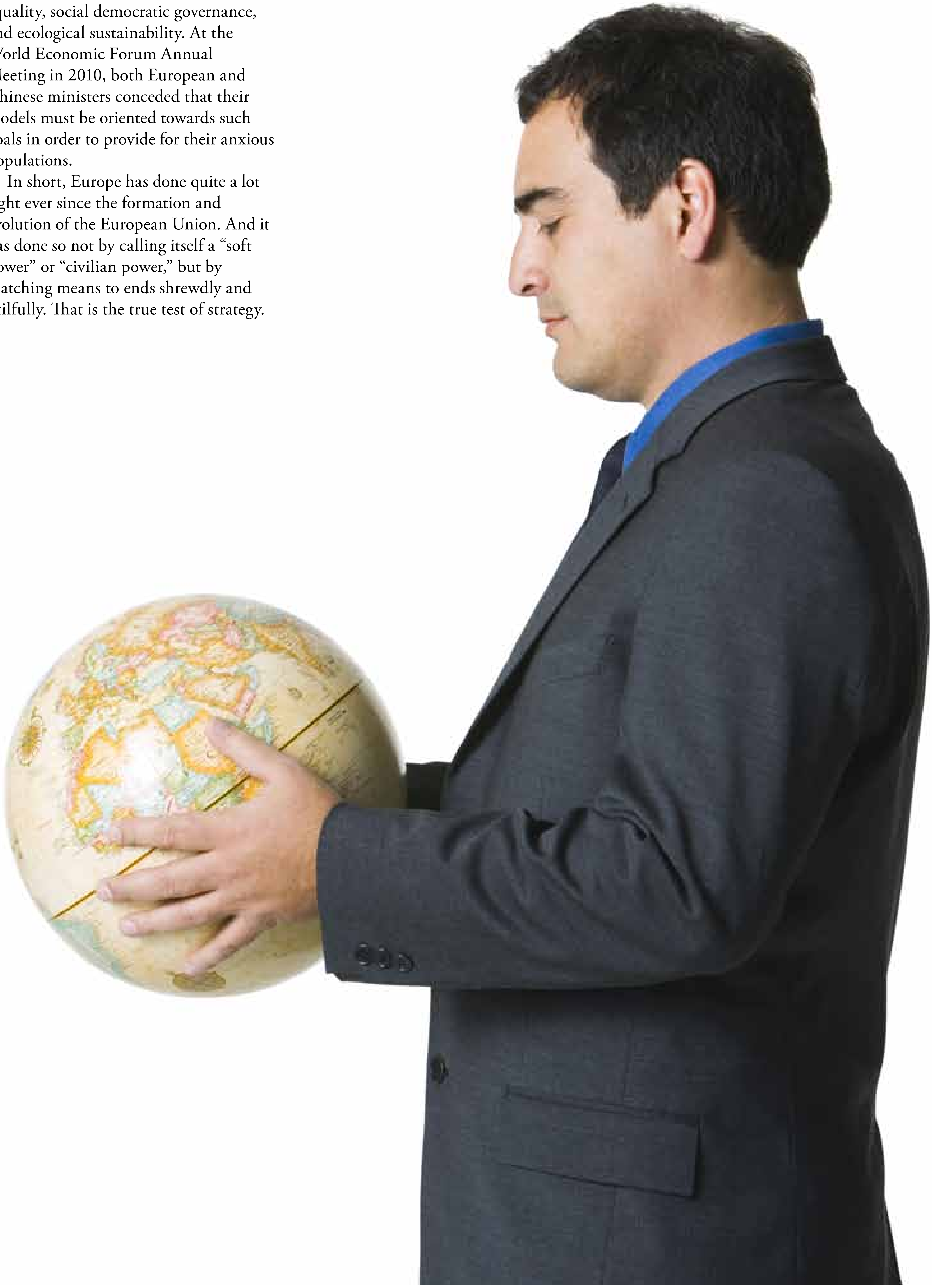
Europe's investments close to home have been crucial to Europe's successful expansion politically and economically, and must continue even as the common European house grows. As new European members secured market access, participation in the Schengen zone, official cohesion funds and subsidies, and improved credibility among creditors and investors, they quickly became the fastest growing nations in Europe until the onset of the financial crisis in 2008-9. But the lessons from that crisis are that EU member-states—new and old—have become interdependent and must support each other for collective gain.

It may seem the height of folly to encourage Europe to take on ever more burdens through continued expansion of the EU, but bear in mind that calculations of global power frequently hinge on demographic size and economic growth—hence some such lists tend to leave off Europe entirely while focusing on China and India. This is their mistake—and Europe's for not acting as one and investing in future growth. An EU that deepens ties with and eventually comes to include Ukraine and Turkey will add close to 150 million largely young, educated and industrious citizens to its labour force, while simultaneously deepening its access to the markets and resources of the Near East and Russia. Deeper economic engagement with North Africa will also bring a Mediterranean Union to fruition faster than political overtures, while also expanding the European sphere of influence. The dictum that must always lead European thinking is that "There is no Europe, only Europeanization."

To act as one Europe will mean consolidating European seats in major international organisations such as the United Nations Security Council and International Monetary Fund. This recommendation, which has been talked about a lot in recent years, has been met with resistance from some EU member states in the name of maintaining influence in these organisations. But this counter-argument is deeply flawed. First, the lack of reform renders such bodies illegitimate, meaning Western powers may eventually stand alone in them, ultimately influencing no one. Second, precisely because the EU lacks the combined strategic capabilities of coercion outside of its immediate theatre, it very much relies on diplomatic manoeuvring in representative multilateral organisations. Creating space in such bodies for new members thereby also creates more—not less—opportunities for Europe to influence their behaviour.

Despite the setbacks the eurozone faces with the crises in Greece and Ireland, the "European Model" is still a global standard bearer on many levels. Europe continues to represent both the aspiration and reality of nearly universal healthcare provision, low-income equality, social democratic governance, and ecological sustainability. At the World Economic Forum Annual Meeting in 2010, both European and Chinese ministers conceded that their models must be oriented towards such goals in order to provide for their anxious populations.

In short, Europe has done quite a lot right ever since the formation and evolution of the European Union. And it has done so not by calling itself a "soft power" or "civilian power," but by matching means to ends shrewdly and skilfully. That is the true test of strategy.



References and Additional Reading

- Accenture. *New Waves of Growth: Unlocking Opportunity in the Multi-Polar World* (London: Accenture, 2011)
- Barroso, José Manuel. *Political Guidelines for the Next European Commission* (Brussels: European Commission, 2009)
- European Commission. *Europe 2020: A European Strategy for Smart, Sustainable and Inclusive Growth* (Luxembourg: European Commission, 2010)
- —. *Europe 2020 Flagship Initiative: Innovation Union* (Brussels: European Commission, 2010)
- González, Felipe et. al.. *Project Europe 2030: Challenges and Opportunities. A Report to the European Council by the Reflection Group on the Future of Europe* (Brussels: May, 2010)
- Hofheinz, Paul. *Europe 2020: Why Skills are Key for Europe's Future* (Brussels: The Lisbon Council, 2009)
- Khanna, Parag. *How to Run the World: Charting a Course to the Next Renaissance* (New York: Random House, 2011)
- —. *The Second World: Empires and Influence in the New Global Order* (New York: Random House, 2008)
- Kok, Wim et. al.. *Facing the Challenge: The Lisbon Strategy for Growth and Employment* (Brussels: European Commission, 2004)
- Legrain, Philippe. *Beyond CAP: Why the EU Budget Needs Reform* (Brussels: The Lisbon Council, 2010)
- Leipold, Alessandro. *Good Governance for the Euro Area: Proposals for Economic Stability* (Brussels: The Lisbon Council, 2010)
- —. *Preventing Greek Tragedy from Becoming a Eurozone Disaster* (Brussels: The Lisbon Council, 2010)
- Mettler, Ann. *From Why to How: Reflections on the Lisbon Agenda Post-2010* (Brussels: The Lisbon Council, 2008)
- —. *A New Dawn: Ten Recommendations for the New European Commission* (Brussels: The Lisbon Council, 2009)
- —. *Innovating Indicators: Choosing the Right Targets for Europe 2020* (Brussels: The Lisbon Council, 2009)
- —. *If Not Now, Then When? Using Europe 2020 to Move from Crisis Management to Restoring Confidence and Growth* (Brussels: The Lisbon Council, 2010)
- Monti, Mario. *A New Strategy for the Single Market: Report to the President of the European Commission* (Brussels: European Commission, 2010).
- Mulgan, Geoff. *The Art of Public Strategy: Mobilising Power and Knowledge for the Common Good* (Oxford: Oxford University Press, 2008)
- Mulgan, Geoff, Neil Reeder, Mhairi Aylott and Luke Bo'sher. *Social Impact Investment: The Opportunity and Challenge of Social Impact Bonds* (London: Young Foundation, 2010)
- OECD. *PISA 2009 Results: What Students Know and Can Do* (Paris: OECD, 2010)
- Williams, Anthony D.. *Wikinomics and the Era of Openness: European Innovation at a Crossroads* (Brussels: The Lisbon Council, 2010)

Acknowledgements
The Lisbon Council would like to thank the European Commission's Education, Audiovisual and Culture Executive Agency for an operating grant which makes possible so much work on the European project. The authors would also like to thank the participants of The Europe 2020 Summit where the conclusions of this policy brief were first presented and discussed, including José Manuel Barroso, president of the European Commission. Special thanks as well to Chris Barton, Bernard Foubert, Raymond Frenken, Britta Jacquet, Nadine Legrand, Stéphanie Lepczynski, Alice M. Schutte-Nahon, Sylwia Stępień, and Caroline De Winter.

Lisbon Council Policy Brief, Vol. V, No. 2 (2011)
ISSN 2031 0943

Published under the editorial responsibility of the Lisbon Council asbl. The responsible editor is Paul Hofheinz, president, the Lisbon Council asbl.

The Lisbon Council for Economic Competitiveness and Social Renewal asbl is a Brussels-based think tank and policy network. Established in 2003 in Belgium as a non-profit, non-partisan association, the group is dedicated to making a positive contribution through cutting-edge research and by engaging politicians and the public at large in a constructive exchange about Europe's economic and social future.

www.lisboncouncil.net

The Lisbon Council asbl
IPC-Residence Palace
155 rue de la Loi
1040 Brussels, Belgium
T. +32 2 647 9575
F. +32 2 640 9828
info@lisboncouncil.net

Design by **www.karakas.be**