UNICE
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The General Assembly of Svenskt Näringsliv

19 May 2005

How to create a World Class Business Climate in Europe

Dr Strube, UNICE President

Ladies and Gentlemen, …

Creative thinking gains much from an inspiring environment. What could be more inspiring for us today than meeting in Stockholm's Moderna Museet – one of Europe's finest art collections?

We are here to reflect on business. What kind of inspiration can we expect from art? There are at least three parallels we can draw between art and business.

First and obviously, both require creative minds. Secondly, it is true for both that competition is the whetstone of talent. And thirdly, in both fields, excellence is a question of focusing on the essential and eliminating the unnecessary.

My question today is "How to create a World Class Business Climate in Europe". On first sight, the answer seems to be clear: By putting together the success ingredients we already have at hand. That is, in some parts of the European economy we do have a world-class business climate and globally successful companies. And finally, Europe has an excellent program to become the top World Class Region by 2010: The Lisbon Strategy.

Unfortunately, reaching the top in the economic world champions league is not as simple as that. Two months ago, European heads of State carried out the mid-term review of the Lisbon Strategy five years after they had proclaimed it. They managed to agree on the obvious analysis that Europe's economy, as a whole is off track. However, apparently, it was politically not feasible to face the facts and to draw the policy consequences. Myopic political considerations such as the forthcoming referendums on the European Constitution have prevented Member States to focus EU economic policy on what Europe really needs: growth and jobs.

On a national level, some positive reforms to improve the business climate took place in the last five years. However, we have to face the fact that most of the implemented reforms are too little, too slow. As a result, low growth and high unemployment hit the front pages in Europe, whereas for many other economies last year's growth rates were the highest in decades. Moreover, confidence in future growth prospects for the EU is waning again. In recent weeks, the growth outlook for this year was slashed, especially in the Eurozone, where it is currently expected to be even less than last year's lacklustre 1.8%. The outlook is rosier however for many new Member States and also for Sweden (+ 2,7% in 2005).

Union of Industrial and Employers' Confederations of Europe – Union des Confédérations de l'Industrie et des Employeurs d'Europe AISBL
Av. de Cortenbergh 168 - B-1000 Brussels -VAT BE 863.418.279 -Tel. +32(0)2 237.65.11 - Fax +32(0)2 231.14.45 - E-mail: main@unice.be -Website: //www.unice.org

So Europe as a whole is far from playing on a world-class level although we have the strength and the potential to do so. A key comparative advantage of Europe could be its diversity and creativity. It is the great variety of European languages, cultures and landscapes that make our continent so fascinating.

We also can find a variety of creative and successful structural reforms in Europe, for example, the pension reform in Sweden. European governments have the excellent opportunity to learn from each other and pick up the best approach. Unfortunately the European Council has not agreed on “best practice” as a key element in the relaunch of the Lisbon Strategy.

Furthermore, we have some excellent global players on our continent. Examples like IKEA’s furniture, Italian designer products or Swiss watches show that Europe is able to gain competitive edges on a global level. Let’s take a look at other economic sectors where Europe can outperform its global competitors:

The automotive sector has been providing growth and jobs to Europe. In Germany alone, some €110 billion has been invested in auto R&D over the past ten years. Europe is the largest automotive production region and a competence leader for building world-class premium cars. A total of 10 mio. people are directly or indirectly employed in this sector. Of course, one should never rest on one’s laurels. The automotive sector is also facing important challenges. To address these and ensure its future competitiveness, the European Commission has launched a promising initiative with the European automotive sector called "cars 21".

The European chemical industry is able to defend its strong position on world markets by carrying out substantial structural changes as more and more important customers are shifting their productions to the new growth regions, especially in Asia. Future challenges are low market growth in Europe and rising import pressure in commodities from Asia and countries with low cost feedstock.

European pharmaceutical companies are also world-class but the lack of a favourable climate for innovation and price controls have driven more and more activities to the US.

High-technology firms, like Nokia, Philips or Siemens are increasingly developing and producing their products in emerging markets such as China.

In international benchmark rankings on competitiveness the EU Member States show a mixed performance. The Nordic countries are regularly rated among the most competitive in the world whereas important economies like France, Germany or Italy hold low positions. However, when it comes to the competitiveness of their companies they are ranked on top places. Indeed, most of the big European transnational companies and many SMEs are world-class global players.

Successful sectors are competitive by increasing their activities all over the world.

Relocation of production within the global value chain is "natural", so to say, and part of the global process of increased division of labour. Cost efficient productions in Eastern Europe or third countries maintain or even strengthen the competitiveness of local productions in Western Europe: The VW Golf with standard equipment costs about 17.000 €; if it were completely manufactured in Germany, including all components, it would cost about 32.000 € and would be unsellable.

It is also "natural" that companies go where markets are growing, and markets in emerging economies are growing faster than here, because they start from a much lower base. It would be illusionary to expect growth rates of 9% as in China or India for the EU. In the coming decades, Europe’s population and therefore its market potential will be shrinking. But Europe can, and indeed does, profit from growing markets elsewhere. The Chinese boom has substantially contributed to the economic growth in Europe. Therefore, it is in Europe’s interest to continue opening up world trade and ensure that our goods, services and investments have a free access to markets outside our borders. Protectionism is not the way forward. The openness of the Swedish economy is certainly a key success factor of your country.

Although companies and individual Member States must find their own way in succeeding in global competition there are some common challenges to which, sooner or later, all European countries will have to respond. Let me name four of them:

1) All European countries will have to develop their <u>innovative capacity</u> in high quality and high technology products and services. None of the EU Member States will be able to compete only on low production cost. Therefore, it is essential to invest in effective research. Sweden is among the world leaders in that respect, with an R&D spending of more than 4% of GDP. However, the bulk of R&D expenditure in Sweden comes from only a handful of big, innovative companies.

The European Union can and must be an important catalyst to stimulate research and innovation. In that respect, the Seventh EU Research and Development Framework Programme, recently published by the Commission, represents a step towards making research and development a more effective contributor to innovation in Europe.

However, spending more on R+D is a means to an end and not an end in itself. We also need a different mind-set in our society: We need a positive attitude towards technological innovation, an attitude that focuses on identifying and using opportunities while managing risks. And we need to realize that the price a society has to pay for trying to avoid any risk at any cost is much too high: Ultimately, it will put at risk its own future existence.

Especially for new products, the European legislator is focusing primarily on the potential risks and less on their benefits. This tendency towards overregulation mainly results from the perceived sceptical attitude of the European consumers towards certain innovative products, for example genetically modified food. Creating a positive climate towards innovation in Europe is a challenge for politicians, entrepreneurs, the media and researchers.

Research is only a necessary, not a sufficient condition for gaining a competitive edge in highly sophisticated products and services. It is symptomatic that the highly successful MP3 format (data reduction by perceptual coding techniques) was invented in Europe, but commercialized in the US. Research must be turned into profitable products in order to create growth and jobs. A raft of policy measures is needed to make this happen, starting with an entrepreneurial education in school, developing closer business-science relations, reducing bureaucracy and red tape and providing good conditions for innovative start-ups. But first of all we need a climate conducive to entrepreneurship. And Europe must become more attractive for foreign investors. The current all-time low business investment level in Europe shows that there is work to do in this respect.

To stimulate innovation, the EU has launched a promising initiative: the Competitiveness and Innovation Framework Programme. UNICE is following this initiative closely. Business must make sure that it does not become a "paper tiger", but that it will provide real added value for companies.

2) The EU institutions can do their share to improve the regulatory framework for innovation and entrepreneurship in Europe. Over the years there has been a great deal of lip service to improving the regulatory environment. Companies often have the impression that they will never be able to keep up with the constant flow of new rules. UNICE uses Gulliver as a symbol for the perception of many entrepreneurs and innovators to be tied down by too many rules, regulations and restrictions.

Europe is "world class" when it comes to social policy and environmental protection. In the past 10 years more than 500 EU environmental directives and regulations have been adopted. Stifling innovation by threatening to impose new bureaucratic legislation such as REACH in its present form is not the way to inspire confidence in Europe’s future business climate. In March the "Alliance for a Competitive Europe" which brings together UNICE and 11 federations from European manufacturing industry, has put forward its recommendations for a well founded impact assessment of legislative initiatives. UNICE is strongly supporting Commissioner Verheugen’s recent initiative to simplify existing EU legislation and to screen pending proposals. It is now high time for better results of “better regulation”!

3) Michael E. Porter has drawn our attention to the fact that some key factors ("diamonds") are necessary to create competitive advantages: industrial clusters, strong local roots and intensive competition. Therefore, we must continue, as a top priority, to strengthen our "home market", the EU internal market. The Single Market is not "yesterday’s business", as it is often perceived in public opinion. Without doubt it is a "World Class Market" and the model for many integration processes in other parts of the world, e.g. in Latin America.

Currently, the liberalisation of services is the most important policy measure the EU can enact to complete the internal market and to improve the business climate in Europe. Unfortunately, the debate has been hijacked by emotional arguments on "social dumping", many of them unfounded. UNICE agrees that the Directive must not undermine existing legislation on posting of workers. But this can be ensured, and must not be a reason to delay the creation of an Internal Market for services.

4) Labour markets are primarily a national responsibility. In order to foster jobs and growth, the EU should refrain from imposing additional rules on national labour markets. However, the new EU Social Policy Agenda, recently presented by the Commission seems to reveal a different intention. We do not need an additional layer of EU collective bargaining above the national, sectoral, regional or company level. This proposal along with many others of the

Social Policy Agenda contradict the Lisbon objective. The Commission is walking a very thin line; it must prove that it is serious with its initiative on growth and jobs.

The most important decision taken at the European Council in March was the commitment by all Member States' governments to draw up "National Action Programmes" for reform. UNICE Member Federations have been very active in pushing for these National Action Programmes ahead of the European Council. Swedish Enterprise among them has sent a letter to Prime Minister Persson calling for four challenges to be addressed in the Swedish action programme: reduce tax burden on labour and enterprise, improve the investment climate, create a more flexible and efficient labour market and promote an entrepreneurial climate that is more supportive to start-ups. High-taxes and an expensive welfare state are not conducive to attract people into starting their own business.

To help regain credibility and momentum of the Lisbon Strategy the EU and the Member States have to speed up the structural reforms and secure an "early harvest" of quick wins in 2005. This means identifying a handful of practical and realistic priorities, where progress can be achieved by year-end.

Should the Constitutional Treaty not be ratified in the French referendum on 29 May or in subsequent referendums, it would be much more difficult for the EU to create sufficient momentum for economic reform projects, on European as well as on national level. A non-ratification would make any EU action much more difficult. The Treaty provides the EU with a governance system that strengthens the decision-making process of European Institutions with 25 Member States. But it neither makes the EU more "neoliberal" nor more "social" and it will not stop globalization. It simply makes the EU more efficient. We will not get a more competitive, a more social and a more sustainable Europe through a "NON" in France. We all should do what we can to explain what the Constitutional Treaty is all about and thus help avoiding a European policy set-back.

You are probably aware that the German Parliament approved the Constitutional Treaty last week with a large majority of votes and that during the month preceding elections in Northrhine-Westfalia, Mr Müntefering, the head of our Socialdemocrats, has initiated a debate on capitalism. The critique of capitalism gained far more public attention than our Parliament's approval of the Treaty. It is safe to assume that very few people have read the Treaty or have paid attention to this topic whereas Mr Müntefering's graphic description of "predatory capitalists invading the country like locusts" appealed to emotions shared by many. In public opinion: the Treaty is a topic for experts if it is known at all that it exists, but the sense of being overwhelmed by Change, of being threatened and exposed, of feeling "Angst" is shared by a large majority of the electorate in Germany, France, the Netherlands and so on.

I am convinced that building confidence in the EU, in the market economy, free enterprise and individual freedom, all necessary for our sustainable development, requires a major long-term effort above and beyond the ratification process of the Constitutional Treaty. Can Europe cope with these challenges without a period of consolidation?

We aim to create a world class business climate in Europe – so what kind of inspiration can we get from the field of art in order to be successful? The way I see it, we should draw three lessons from the great works of art collected here.

First lesson: *creativity* – that is, encourage innovative thinkers and processes. For innovation is key to Europe's future success.

Second lesson: *competition* – that is, enhance competitiveness by fostering an entrepreneurial spirit.

Third lesson: *concentration* – that is, focus economic policy on two top priorities: growth and jobs.

Creating a world-class business climate is a work of art – balancing hard facts, soft factors, inspiration and confidence in our ability to shape our future.

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