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Address by UNICE President Ernest-Antoine Seillière “The innovation challenge in Europe”

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Ladies and Gentlemen,

It is a great a pleasure to address this conference and bring, as president of UNICE, a European dimension to this morning's debate, which focuses on competitiveness and innovation.

We have just heard Minister Joan Clos discussing the Spanish economic model and how to improve it to support continued and balanced growth in the years ahead.

At the outset, it is good to remind ourselves that Spain is one of the best examples of what European integration is about: convergence of living standards through market opening, structural reforms and sound macroeconomic policies.

This year, GDP per capita in Spain will for the first time come into line with the EU average, while it was still 13% below it only a decade ago. That can be described as fast convergence.

But at the same time, Spain also encapsulates the many challenges that Europe as a whole is currently facing.

First of all, despite a steep downward trend, high structural unemployment has not been resolved. Second, Spain is struggling to improve productivity, which is stalling despite strong economic growth. Third, and this is of course related, Spain has lost important competitiveness ground against its main trading partners and its current account deficit is reaching alarming levels.

So, I would say that it is not only convergence of living standards that we are observing between Spain and the EU, but also of policy priorities. Let me elaborate in particular on productivity and competitiveness.

As with Spain, Europe is stuck in a weak productivity growth regime, while we can argue that opportunities have rarely been so abundant. In fact, we see in other parts of the world what fast globalisation and technological progress can bring in terms of productivity advances.

In Europe, the picture is much less encouraging. Despite the current recovery, UNICE estimates that labour productivity per hour worked will remain at around 1.5% this year and next, in line with the poor average performance of the last decade. This is a major factor hampering growth prospects and our capacity to face the challenges ahead, including of course demographic ageing.

What is our problem? In a few words, Europe continues to have the institutions and policies of a “catching-up” economy inherited from 60s and 70s, when its growth was driven by accumulating capital and by imitating or adapting technologies developed elsewhere (the US or Japan).

But Europe is now at the world’s “technology frontier”, and its growth relies more and more on its capacity to cross this frontier and to adapt to fast economic changes. This is what Europe is still not very good at and where it should concentrate its efforts.

There are four areas of improvement that are particularly crucial to build up a Europe of innovation: competition, technological infrastructures, education and flexible labour markets.

1. Competition

The importance of the regulatory environment in either hindering or fostering innovation cannot be denied.

The productivity growth advantage experienced by the United States and the best performing EU countries shows in this regard how low barriers to competition and entrepreneurship can stimulate investment, innovation and the dissemination of new technologies (Nicoletti and Scarpetta - OECD (2005)).

Recent economic research also demonstrates that the cost of insufficient competition and over-regulation increases as an economy, or an industry, moves closer to the technology frontier (Philippe Aghion - Harvard University (2006)).

What does that tell us about the future direction of EU policies? First, that it is crucial to put the internal market back at the centre of the policy agenda, and to make competition a reality, particularly in the field of services, energy and capital markets.

Second, that we need effective implementation of better regulation initiatives at both EU and national level, bearing in mind that SMEs are the backbone of Europe’s innovation potential and also the first victims of over-regulation.

But progress on simplification of EU regulations and impact assessments is far from satisfactory, despite all the Commission’s laudable intentions.

2. Technological infrastructures

Europe must actively develop a strong research and technology base. The EU currently spends 1.9% of its GDP on R&D expenditure and 2.6% on Information and Communication Technologies (ICT). This does not compare favourably with figures in the US, of 2.7% for R&D and 3.8% for ICT respectively.

Among the reasons why the EU lags behind, we can mention the fragmentation of research activities, an ineffective link between the public and private sector, and the lack of an efficient intellectual property system.

We need to reconsider and promote the concept of public-private partnership in innovation. This should include partnership in setting the agenda for education, research and other innovation-supporting measures.

The European Technology Platforms (ETPs) and Joint Technology Initiatives (JTIs) to be set up under the Seventh Research Framework Programme are both examples of public-private partnerships with great potential.

Regarding the proposed European Institute of Technology (EIT), business wants it to be an effective lever to bring together research, innovation and education, but it is important that its financing does not come at the expense of other EU research or lifelong learning programmes, and that a strong link with the private sector can be established.

A strong intellectual property system would also be a major contribution to reinforce Europe's R&D and innovation. UNICE is strongly in favour of having a Community patent, and we stress the need to have a system that is both user-friendly and based on a reliable legal system.

3. Education, education, education

An essential and mandatory pillar to foster productivity in a knowledge-based economy is the development and management of human capital.

Europe needs to increase both educational attainment levels and improve access to lifelong learning. Together with the need to invest more, a stronger effort needs to be made to increase the effectiveness of spending. Key priorities are to:

- ensure that individuals acquire the necessary basic skills;
- invest more in higher education;
- facilitate companies investment in human capital;
- ensure that education and training match the needs of companies;
- encourage individuals to take responsibility for upgrading their competences;

4. Flexicurity

Innovation also comes with modern work processes and there is undoubtedly a link to be made between the flexicurity debate and the European productivity challenge.

Many European decision-makers are conscious that outdated and unnecessarily rigid labour regulations hamper businesses development and curb productivity growth. Most people agree that high labour taxation and lack of mobility increase the adjustment costs associated with globalisation and technological innovations. Many even acknowledge, at least in theory, that hours worked per person employed have declined dangerously in the face of demographic ageing.

However, when it comes to drawing the consequences of this analysis and deciding on reforms, things are much less consensual. Fears and resistance, especially in some big EU countries, are considerably slowing down necessary measures. There is not enough awareness that time is running out and that the longer they are delayed, the more difficult and painful reforms will become.

The flexicurity approach requires comprehensive national strategies including in particular:

- flexible labour laws with smart rules on protection against dismissals;
- effective active labour market policies, which presupposes that the necessary budgetary margins have been created, and
- employment-friendly social protection systems balancing rights and obligations.

Europe can, and must, have both employment and productivity growth in the future if it wants to sustain its social model in an ageing society. But let's not delude ourselves: this will not come without reforms.

The exact nature of these reforms have to be decided at national level, but the European Union also has an important role to play by ensuring that governments live up to their promises, and that there is overall coherence between EU and national policies under the growth and jobs strategy.

Let me conclude by saying a few words on competitiveness and sustainable development.

A generally accepted definition of sustainable development is "development that meets the needs of the present without compromising the ability of future generations to meet their own needs" (United Nations).

A society which strives for sustainable development must therefore pay attention to three dimensions: economic, social and environmental sustainability. It is clear that the last two are conditional on the first.

A case in point is the current debate on climate change. The biggest emitter of greenhouse gases, the US, and the country with the biggest growth rate in greenhouse gas emissions, China, are not taking part in the Kyoto process. Europe cannot play it

alone. Unilateral measures will not solve global environmental issues, while they can certainly hurt the position of European industries in global competition.

The way towards true sustainable development will come through European climate change diplomacy which succeeds in finding a global strategy, including all major players.

Only then will Europe's leadership have a noticeable impact on global environmental protection, and only then will Europe be able to enjoy the competitiveness advantages of its strong eco-innovation industries.

Thank you for your attention.
