# FACING THE CHALLENGE

## The Lisbon strategy for growth and employment

*Report from the High Level Group chaired by Wim Kok*

*November 2004*

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NOVEMBER 2004

# The High Level Group

### Mandate

The Europe Council held in Brussels in March 2004 adopted the following conclusions:

*"The European Council invites the Commission to establish a high-level group headed by Mr Wim Kok to carry out an independent review to contribute to this exercise. Its report should identify measures which together form a consistent strategy for our economies to achieve the Lisbon objectives and targets. The group should be composed of a limited number of highly qualified individuals able to reflect the views of all stakeholders. Its report, which will be made public, is due to be submitted to the Commission by 1 November 2004"*.



### Membership

The Task Force was composed of the following Members

- Mr Willem Kok (Chairman), former Prime Minister of the Netherlands.
- Mr Romain Bausch, President and CEO SES Global.
- Mr Niall Fitzgerald, Chairman of Reuters, Chairman of the Trans-Atlantic dialogue.
- Mr Antonio Gutiérrez, Member of the Spanish Parliament.
- Mr Will Hutton, Chief Executive of the Work Foundation, leader writer.
- Ms Anne-Marie Idrac, Chairwoman of the RATP (Paris public transport system).
- Ms Wanja Lundby-Wedin, Chairwoman of the Swedish Trade Union Confederation.
- Mr Thomas Mirow, Hamburg City Councillor, responsible for economic affairs.
- Mr Bedrich Moldan, Chairman of the Environment Centre (Charles University, Prague).
- Mr Luigi Paganetto, Professor of international economics (Rome-Tor Vergata University)
- Mr Dariusz Rosati, Member of the European Parliament, Professor of economics.
- Mr Veli Sundbäck, Vice-President of Nokia-Finland.
- Mr Friedrich Verzetnitsch, Chairman of the ÖGB trade union.

The High Level Group carried out its work from May to October 2004. It met six times and presented its report to the European Commission on 3 November 2004.

The Secretariat of the High Level Group was held by the European Commission.

# Executive summary

In March 2000 European leaders committed the EU to become by 2010 "the most dynamic and competitive knowledge-based economy in the world capable of sustainable economic growth with more and better jobs and greater social cohesion, and respect for the environment". The Lisbon strategy, as it has come to be known, was a comprehensive but interdependent series of reforms. Actions by any one Member State, ran the argument, would be all the more effective if other Member States acted in concert.

External events since 2000 have not helped achieving the objectives but the European Union and its Members States have clearly itself contributed to slow progress by failing to act on much of the Lisbon strategy with sufficient urgency. This disappointing delivery is due to an overloaded agenda, poor co-ordination and conflicting priorities. However, a key issue has been the lack of determined political action.

The Lisbon strategy is even more urgent today as the growth gap with North America and Asia has widened, while Europe must meet the combined challenges of low population growth and ageing. Time is running out and there can be no room for complacency. Better implementation is needed now to make up for lost time.

In this context, if we are to deliver the Lisbon-goals of growth and employment then we must ***all*** take action. To achieve them will require everyone to engage. This means more delivery from the European Institutions and Member States through greater political commitment; broader and deeper engagement of Europe's citizens and a recognition that by working together Europe's nations benefit all their citizens.

Each element of the Lisbon strategy is still needed for the success of the whole. Improved economic growth and increased employment provide the means of sustaining social cohesion and environmental sustainability. In their turn, social cohesion and environmental sustainability **can contribute to** a higher level of growth and employment.

Thus there is no single action that will deliver the higher growth and jobs. Rather there are a series of interconnected initiatives and structural changes that through concurrent action in the European Union will release its undoubted potential. This requires urgent action across five areas of policy:

**The Knowledge Society** – Increasing Europe's attractiveness for researchers and scientists, making R&D a top priority and promoting the use of ICT.

**The Internal Market** – Completion of the internal market for free movement of goods and capital and urgent action to create a single market for services.

**The Business Climate** – Reducing the total administrative burden, improving the quality of legislation, facilitating the rapid start up of new enterprises; and creating an environment more supportive to businesses.

**The Labour Market** – Rapid delivery on the recommendations of the European Employment Taskforce; developing strategies for life long leaning and active ageing and underpinning partnerships for growth and employment.

**The Environmental Sustainability** –Spreading eco-innovations and building leadership in eco-industry; pursuing policies which lead to long term and sustained improvements in productivity through eco-efficiency.

Individual Member States have made progress in one or more of these policy priority areas but none have succeeded consistently across a broad front. Europe as a whole really wants to achieve its targets, it needs to step up its efforts considerably.

The task is to develop national policies in each Member State, supported by an appropriate European wide framework, that address particular Member State's concerns and then to act in a more concerted and determined way. The European Commission must be prepared to report clearly and precisely on success and failure in each Member State. National and European Union's policies, including their budgets, must better reflect the Lisbon priorities.

In order to ensure that Member States take up their responsibility, a process-redesign is required along three lines: more coherence and consistency between policies and participants, improving the process for delivery by involving national parliaments and social partners and clearer communication on objectives and achievements.

In addition, the High Level Experts Group proposes that:

- The **European Council** takes the lead in progressing the Lisbon strategy.
- The **Member States** prepare national programmes to commit themselves to delivery and engage citizens and stakeholders in the process.
- The **European Commission** reviews, reports and facilitates the progress and supports it by its policies and actions.
- The **European Parliament** plays a proactive role in monitoring performance.



To achieve the goals of higher growth and increased employment in order to sustain Europe's social model, will require powerful, committed and convincing political leadership. Member States and the European Commission must re-double their efforts to make change happen. Far more emphasis must be placed on engaging Europe's citizens with that case for change. Greater focus is required to build understanding of why Lisbon is relevant to every person in every household in Europe.

Europe has built a distinctive economic and social model that has combined productivity, social cohesion and a growing commitment to environmental sustainability. The Lisbon strategy refocused on growth and employment in the way this report suggests offers Europe a new frontier for that economic and social model. A frontier that is based on a thriving knowledge economy, an inclusive society and environmental sustainability.

# Chapter 1 - WHY LISBON?

## INTRODUCTION

In March 2000 the then fifteen EU leaders agreed at the Lisbon Spring Summit that the EU should commit to raising the rate of growth and employment to underpin social cohesion and environmental sustainability. The US economy, building on the emergence of the so-called "new" knowledge economy and its leadership in information and communication technologies (ICT), had begun to outperform all but the very best of the individual European economies. Europe, if it wished to protect its particular social model and continue to offer its citizens opportunity, jobs and quality of life, had to act determinedly – particularly in the context of the mounting economic challenge from Asia and the slowdown of European population growth. The EU set itself "a strategic goal for the next decade: to become the most dynamic and competitive knowledge-based economy in the world capable of sustainable economic growth with more and better jobs and greater social cohesion, and respect for the environment".

Actions by any one Member State, ran the argument, would be all the more effective if all other Member States acted in concert; a jointly created economic tide would be even more powerful in its capacity to lift every European boat. The more the EU could develop its knowledge and market opening initiatives in tandem, the stronger and more competitive each Member State's economy would be. The Lisbon strategy, as it has come to be known, was a comprehensive, interdependent and self-reinforcing series of reforms.

The arguments supporting that strategy are no less compelling today – indeed more so. Europe needs to innovate on its own behalf. The strength of its knowledge industries and Europe's capacity to diffuse knowledge across the totality of the economy are fundamental to its success and are key to lifting its growth of productivity to compensate for falling population growth and pay for its social model. Lisbon should be understood as a means of transitioning the European economy from structures in which it essentially caught-up with the world's best, to establishing economic structures that will allow it to exercise economic leadership.

From the outset the Lisbon reform programme seeks to marry economic dynamism to create higher growth and employment rates with longstanding European concerns to advance social cohesion, fairness and environmental protection. Lisbon aims to raise private and public research and development spending as the centrepiece of a concerted effort to increase the creation and diffusion of scientific, technological and intellectual capital. It aims to foster trade and competition by completing the single market and opening up hitherto sheltered and protected sectors. It aims to improve the climate for enterprise and business. It aims to secure more flexibility and adaptability in the labour market by raising educational and skill levels, pursuing active labour market policies and to encourage that Europe's welfare states help the growth of employment and productivity rather than hinder it. And it aims for growth to be environmentally sustainable.

Success in the knowledge economy was seen as the key to allowing Europe both to remain open and socially cohesive. Europe did not want to compete both internally as an economic union and externally by initiating a race to lower real wage and non wage costs so that

Member States would find their systems of social cohesion, partnership in the workplace and protection of the environment undermined. The more Europe could sustain itself as a high productivity, high value added, high employment economy, the better able it would be to create the wealth and jobs that would allow it both to sustain its vital commitment to open markets and to social and environmental Europe.

The Lisbon strategy is sometimes criticised for being a creature of the heady optimism of the late 1990s about the then trendy knowledge economy, neglecting the importance of the traditional industrial strengths of the European economy. To the extent that Lisbon has been interpreted as undervaluing industry this is a fair criticism. It is vital that Europe retains a strong industrial and manufacturing base as a crucial component of a balanced approach to economic growth. Indeed industrial growth and productivity since industrialisation have always been underpinned by advances in technologies and sectors, and Lisbon is based on this long standing truth. Adversely a vigorous knowledge economy necessarily needs a strong high-tech manufacturing sector making high-tech goods at the frontier of science and technology.

Lisbon, because of the range of its ambition, covered a number of areas in which the EU had no constitutional competence and which were the preserve of Member States. Therefore it was designed to proceed by a combination of the traditional “Community method” of EU legislation brought forward by the European Commission and via a new process known as the “Open Method of Co-ordination”. Under this process Member States agree to voluntarily co-operate in areas of national competence and to make use of best practice from other Member States, but customise it to their particular national circumstances. The European Commission’s role is to co-ordinate this process by ensuring that Member States had full information about each other’s progress and policies whilst making sure that those areas for which it had competence – notably the single market and competition policy – would reinforce the Lisbon goals by application of the Community method. Moreover the Commission monitoring would stimulate and create the necessary peer pressure to achieve these goals by publicising the results achieved by the individual Member States. The Lisbon agenda would thus deliver much needed growth and jobs while requiring Member States voluntarily to co-ordinate their policies.



**Europe in a changed world**

The last four years have not been kind to the chances of achieving the Lisbon goals. The ink had scarcely dried on the agreement before the worldwide stock market bubble imploded, the epicenter of which was the collapse of the overvalued prices of American dot.com and telecom shares amid evidence of financial and corporate malpractice. Skepticism mounted about the potential of the knowledge economy. The US suffered two years of economic slowdown and recession and the European economy followed suit; raising R&D expenditure, for example, is made very much harder in a climate of stagnating output and general pressure on government and corporate budgets.

The terrorist attacks on the US on September 11th 2001 and subsequent events further darkened the international climate. Although governments committed to a further round of trade opening negotiations to boost world trade at Doha, turning intentions into concrete measures has proved stubbornly difficult. There has been a worrying growth in bilateral rather than multilateral trade agreements, and tensions between Europe and the US have resulted in some bitter trade disputes. A growing number of worrying environmental events have further increased the unease about the human impact on world climate. Recently oil prices have increased, due to a combination of increased demand and insecurity surrounding supply, dampening both current economic activity and lowering forecasts for the immediate future. The cumulative impact of all these events has been to sap European consumer and business confidence.

Over the last four years the overall performance of the European economy has been disappointing. The economic upturn in Europe has been weaker than in the US and Asia over the last two years in part because of continuing structural weaknesses and in part because the rate of growth of public and private demand has been low. It is true that Europe's public sector deficits have risen as the so-called automatic stabilizers – rising social security payments and falling tax receipts – have kicked in, but this has been inadequate to counter the cyclical downturn. The room for fiscal maneuver in Europe was limited by the weak budgetary positions with which some European Member States entered the economic downturn, insufficiently consolidating their finances during the previous economic upturn. As a consequence the operation of the Stability and Growth Pact could not sufficiently support growth enhancing macro-economic policies that would have further countered the downward component of the economic cycle.

Thus many Member States have been caught in a conundrum. Because of structural weaknesses and low demand national economic performance has been poor. As national economic performance has been poor, it has been more difficult to implement the Lisbon agenda. It has been harder in this low growth environment for some governments to keep their commitments. They have not taken the execution and delivery of the agreed measures seriously enough. Completing the single market, for example, has not been given the priority it required. This has kept Europe too far from the goals it must reach.



**The mixed Lisbon picture**

At Lisbon and at subsequent Spring Summits a series of ambitious targets[1] were established to support the development of a world beating European economy. But halfway to 2010 the overall picture is very mixed and much needs to be done in order to prevent Lisbon from becoming a synonym for missed objectives and failed promises.

However, despite disappointments Lisbon is not a picture of unrelieved gloom, as some like to paint. There has been a significant progress in employment. European governments have introduced measures that cumulatively have attempted to remove obstacles to the employment of low paid workers, stepped up their active labour market polices, and permitted the growth of temporary employment. The employment rate rose from 62,5% in 1999 to 64,3% in 2003, although not only full-time employment. Seven Member States are set to meet the interim target of 67% by 2005. The overall female employment rate rose to 56% in 2003. Some countries have been successful in implementing policies targeted at raising the employment rates of older workers, now reaching 41.7%.

[1] To monitor the progress on the Lisbon strategy, the Commission and the Council have agreed on a list of 14 indicators. Member States performances on these indicators are shown in annex 1

Furthermore, there has been progress beyond employment. Member States have progressed in the spread of ICT and Internet use in schools, universities, administration and trade. Household internet penetration, for example, has risen rapidly, with twelve Member States meeting the targets.

On a more pessimistic note, net job creation largely stopped in 2001 and the risk is apparent that the 2010 target of 70% employment rate will not be reached. The target of 50% for older workers seems almost out of reach.

On the R&D target, only two states currently have R&D spending exceeding 3% of GDP; in these same two countries business is achieving the goal of spending the equivalent of 2% of GDP on R&D. The rest are behind on both scores. Progress in providing every teacher with digital training is very disappointing. Only five states have exceeded the target for transposing EU Internal Market Directives.

On the environment, the decoupling of economic performance from harmful environmental impacts has been only partly successful. The volume of traffic in Europe is rising more rapidly than GDP and congestion is worsening, as are pollution and noise levels, and continue to damage nature. Most European countries are below their Kyoto targets regarding greenhouse gas emissions with only three countries since 1999 recording visible progress in their reduction.

European enlargement, while a welcome expansion of the EU, has made European-wide achievement of the Lisbon goals even harder. The new Member States tend to have very much lower employment rates and productivity levels; achieving the R&D goals, for example, from a lower base is even tougher than for the EU of the original 15 who signed Lisbon.



**The continued case for Lisbon**

Clearly there are no grounds for complacency. Too many targets will be seriously missed. Europe has lost ground to both the US and Asia and its societies are under strain. It is all the more important that political leaders show the required determination now to take advantage of the current fragile improvement of the economic climate and rise in business confidence to recover as much as possible of the ground lost over the last four years.

Does that mean the ambition is wrong? The answer is no; whether to meet the challenges of enlargement, an ageing population or the rise of the Asian economy – let alone the need to lower current levels of unemployment - ambition is needed more than ever. Is Lisbon over-ambitious? Again no, even if every target were to be hit on schedule, Europe would not be on safe ground. Competitor countries and regions are moving on as well, threatening Europe's position in the global economic league table. Europe must find its place in a global economy, which will nonetheless enable it to uphold its own distinctive choices about the social model that it wants to retain. Whether it is life expectancy, infant mortality rates, income inequality or poverty, Europe has a much better record than the US. The objective of Lisbon is to uphold this record in an environment where the challenges are multiple and growing.

Should the 2010 deadline be lifted? Again no. The 2010 deadline is important for signaling and reinforcing the urgent need for action. Setting a new, later deadline would imply that the situation is now less urgent and thus would be wrong. The ongoing challenge of the 2010 deadline is needed to galvanize Member States to make serious efforts at improvement. In any case Lisbon should not be regarded as a one-off objective to be disregarded after 2010 even if every target had been achieved. It is an ongoing process aimed at securing Europe's future as a high productivity, high value added, high employment and eco-efficient economy. The process will never end on a single date; rather it will be subject to continual renewal, reappraisal and recommitment.

The Lisbon strategy is not an attempt to become a copy-cat of the US – far from it. Lisbon is about achieving Europe's vision of what it wants to be and what it wants to keep in the light of increasing global competition, an ageing population and the enlargement. It has the broad ambition of solidarity with the needy, now and in the future. To realize this ambition Europe needs more growth and more people in work.



## External Challenges – between a rock and a hard place

International competition is intensifying, and Europe faces a twin challenge from Asia and the US. The potential rapid growth of the Chinese economy will create not only a new competitor to Europe, but also a vast and growing market. For Europe to take advantage of the opportunity it needs to have an appropriate economic base, recognising that over the decades ahead competition in manufacturing goods at home and abroad, especially those with a high wage content and stable technologies, is going to be formidable. Indeed China, industrialising with a large and growing stock of foreign direct investment together with its own scientific base, has begun to compete not only in low but also in high value added goods. Although Chinese wages are a fraction of those in Europe, it is clear that the difference in quality of goods produced in China or the EU is already small or non-existent.

India's challenge is no less real – notably in the service sector where it is the single biggest beneficiary of the 'offshoring' or 'outsourcing' of service sector functions with an enormous pool of educated, cheap, English speaking workers. Asia's collective presence in the world trading system is going to become more marked.

Europe has to develop its own area of specialisms, excellence and comparative advantage which inevitably must lie in a commitment to the knowledge economy in its widest sense - but here it is confronted by the dominance of the US. The US threatens to consolidate its leadership. The US accounts for 74% of top 300 IT companies and 46% of top 300 firms ranked by R&D spending. The EU's world share of exports of high tech products is lower than the US; the share of high tech manufacturing in total value-added and numbers employed in high tech manufacturing are also lower. In a global economy Europe has no option but radically to improve its knowledge economy and underlying economic performance if it is to respond to the challenges of Asia and the US.

## Internal Challenges – the greying of Europe

Two forces – declining birth rates and rising life expectancies – are interacting to produce a dramatic change in the size and age structure of Europe's population. The total population size is projected to fall by 2020[2]. By 2050, the working-age population (15-64 years) is

[2] "Budgetary challenges posed by ageing populations", EPC/ECFIN/655/01 2001

projected to be 18% smaller than the current one, and the numbers of those aged over 65 years will have increased by 60%. As a result, the average ratio of persons in retirement compared to those of the present working age in Europe will double from 24% today to almost 50% in 2050. This dependency ratio will vary in 2050 from 36% in Denmark to 61% in Italy.

This development is already at work and in 2015 the EU-average dependency ratio will increase to 30%. The impact is then compounded by the low employment rate of elder workers. These developments will have profound implications for the European economy and its capability to finance the European welfare systems. Ageing will raise the demand for pensions and health care assistance at the same time as it reduces the number of people in working age, to produce the necessary wealth.

European Commission projections[3] estimate that the pure impact of ageing populations will be to reduce the potential growth rate of the EU from the present rate of 2-2.25% to around 1.25% by 2040. The cumulative impact of such a decline would be a GDP per head some 20% lower that could otherwise be expected. Already from 2015, potential economic growth will fall to around 1.5% if the present use of the labour potential remains unchanged.

This same ageing will result in an increase of pension and health care spending by 2050 varying between 4-8% of GDP[4]. Already from 2020 projected spending on pension and health care will increase by some 2% of GDP in many Member States and in 2030 the increase will amount to 4-5% of GDP. On top of this, the lower economic growth rate will impact negatively on public finances, and this negative impact will commence from 2010.



**The challenge of enlargement**

Enlargement has made inequality and problems of EU cohesion more pronounced: the EU population has increased by 20% while the addition to European GDP is only 5%, resulting in a drop of output per head of 12.5% in the EU-25. Moreover, the new Member States are characterised by strong regional disparities with wealth concentrated in a small number of regions. The population living in regions with output per head of less than 75% of the EU has increased from 73 million to 123 million.

Equally, as noted earlier, the EU-25 will find some of the Lisbon targets even more challenging than the EU-15. For example the employment rate has dropped as a consequence of enlargement by almost 1.5 percentage points to 62.9% in 2003. The long-term unemployment rate for the EU-25 is 4% compared to 3.3% for EU-15. Some of the environmental targets will also be more difficult to achieve. On some other indicators (e.g. R&D spending as a share of GDP) the new Member States will need to step up their efforts considerably. However their low economic weight means the overall impact on the EU aggregate target is small.

The positive aspect of enlargement is that it offers the prospect of the new Member States achieving rapid rates of growth in GDP and productivity as they catch up with the European average, so creating an area of economic dynamism in Eastern Europe. There is already evidence that this is happening: output and productivity growth in Estonia, Lithuania, Latvia,

[3] "The EU Economy: 2002 review", European Economy n° 6/2002 p. 192
[4] "The Impact of ageing populations on public finances", EPC/ECFIN/407/04 2003

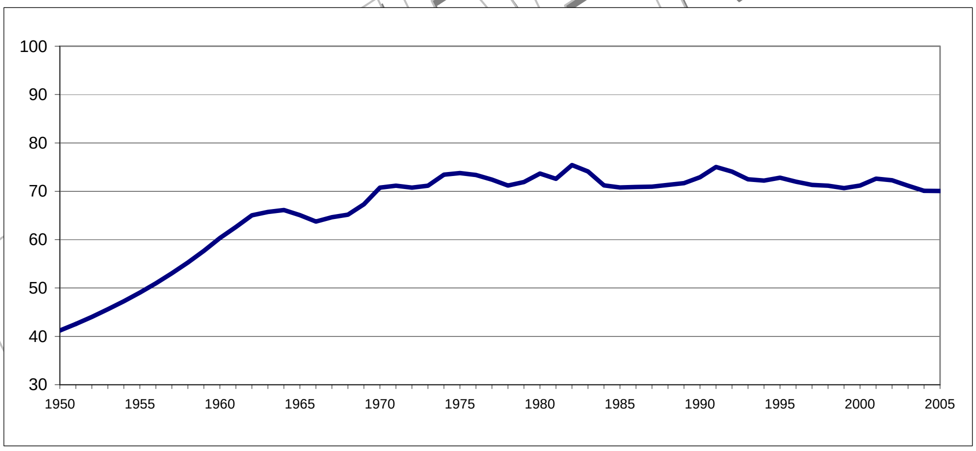
Hungary, Poland, Slovenia, Slovakia and the Czech Republic have been above that of the US over the last five years. As they replace redundant ageing technology with state of the art processes they will jump a generation in terms of their technological capacity; there is every prospect of their growth in output and productivity continuing.

Nonetheless, their low tax and wage rates attracting inward investment from the rest of the EU are likely to be a source of growing friction; unless there is some prospect of convergence these tensions will mount. In this respect meeting the Lisbon goals to promote growth and employment in all parts of the EU is vital for its future internal cohesion.

**The facts on growth, employment and productivity**

Europe's economy, bluntly, is growing less quickly than the US and suffering recently from a lower rate of productivity growth. The post-war catching-up process of the EU with the US in terms of output per head had come to an end in the mid 1970s (see figure 1) but then broadly stabilised. However since 1996 the average annual growth in EU output per head has been 0.4 percentage points below that of the US. From holding its own, Europe is now losing ground.

Figure 1: EU GDP per capita in PPS (at constant 1995 prices) (US=100)

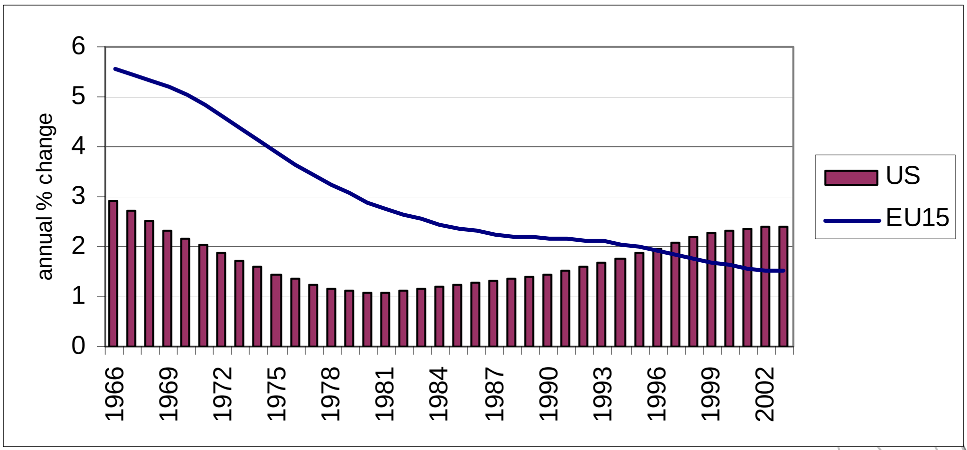



Source: Commission services, 2004-2005: forecasts.

This adverse trend in the growth rate of output per head has been accompanied by a reversal in Europe's productivity catch-up with the US. For the first time in decades, the labour productivity in the EU is on a trend growth path which is lower than that of the US. Over the period 1996-2003, the EU-15 productivity growth rate[5] averaged 1.4%, as opposed to 2.2% recorded for the US.

[5] Given the generally higher dynamics of the new Member States, the EU-25 average productivity growth was slightly higher over this period at 1% but still far behind that in the US.

Figure 2: Labour Productivity Per Hour Growth (moving average)




Source : EU Commission, AMECO database

The decline in EU labour productivity growth rates in the mid-1990s can be attributed more or less equally to a lower investment per employee and to a slowdown in the rate of technological progress. The former can be partially explained by the EU's recent success in employment generation, but the counter-argument is that these newly created jobs tend to be low-productivity jobs.

The latter has been associated with the same reasons Europe is not meeting the Lisbon targets: insufficient investment in R&D and education; an indifferent capacity to transform research into marketable products and processes and the lower productivity performance in European ICT producing industries (including office equipment and semiconductors) and in European ICT using services (such as wholesale and retail trade, financial service) due to a slower rate of ICT diffusion. As a result, the contribution of ICT to growth was half that observed in the US. This performance is also linked to Europe's industrial structure, which is based on more low and medium-tech industries and its difficulty in moving in to those sectors with high productivity growth prospects.

In the latter part of the 1990's the EU experienced an increase in the aggregate numbers of yearly hours worked in contrast to the previous decade. The increase was mainly due to an increase in the number of jobs created, whereas the actual average annual hours worked per person continued to decline. Since 1983 the average hours worked per person has not only decreased more than in both the US and Japan, but it has also run constantly at a lower level due to lower weekly working time and a lower number of working days. To provide a positive contribution to the growth of output per head, a better utilisation of labour is needed, both by increasing employment and by working more hours on a life time basis.

The recent employment growth in Europe, remarked on earlier, has been associated with a *decline* in hourly productivity growth while in the US, the growth in employment has been associated with an *increase* in hourly productivity. If Europe wishes to increase its living standards, it needs to accelerate employment and productivity growth via a wide range of reform policies together with a macro-economic framework supportive of growth, demand and employment.

**Act focused; act together; and act now.**

At risk - in the medium to long run - is nothing less than the sustainability of the society Europe has built. Europeans have made choices about how to express the values they hold in common – a commitment to the social contract that underwrites the risk of unemployment, ill-health and old age and provides opportunity for all through high quality, education; a commitment to public institutions, the public realm and the public interest; and that a market economy should be run fairly and with respect for the environment. These values are expressed in systems of welfare, public institutions and regulation that are expensive in a world where low cost and highly efficient producers are challenging the old order. If Europe cannot adapt, cannot modernise its systems and cannot increase its growth and employment fast enough then it will be impossible to sustain these choices. Europe, in short, must focus on growth and employment in order to achieve the Lisbon ambitions.

The Lisbon strategy was and is Europe's best response to these multiple challenges. It represents a framework of ambition and targets which set out the broad direction of necessary change to sustain an European economy that is genuinely innovative, operates at the frontiers of technology and creates the growth and the jobs that Europe needs. The view of the High Level Group is that Lisbon's direction is right and imperative, but much more urgency is needed in its implementation – and more awareness of the high cost of not doing so.

The problem is, however, that the Lisbon-strategy has become too broad to be understood as an interconnected narrative. Lisbon is about everything and thus about nothing. Everybody is responsible and thus no-one. The end result of the strategy has sometimes been lost. An ambitious and broad reform-agenda needs a clear narrative, in order to be able to communicate effectively about the need for it. So that everybody knows why it is being done and can see the validity of the need to implement sometimes painful reforms. So that everybody knows who is responsible.

To restate, Lisbon is about Europe becoming a single, competitive, dynamic knowledge based economy that is among the best in the world. It wants to embed Europe's commitment to social cohesion and the environment in the core of the growth and jobs generation process so they are part of Europe's competitive advantage. And this can not be done against a background of stagnating or slowly rising demand; the wider macro-economic framework, both the pursuit of monetary and fiscal policy, must be as supportive of growth as possible. In light of this, the High Level Group supports the recent proposed reforms by the European Commission of the Stability and Growth Pact. These reforms offer the flexibility to pursue economic policies that lessen the impact of the economic cycle without loosing sight of the importance of stability. Strengthening governments' fiscal positions in the current upturn, although fragile, is required in order to have more latitude in any subsequent downturn with increased spending or sustainable tax cuts. The need is to create the capacity that will give business the confidence to invest and innovate in the knowledge that the over-riding objective is to sustain the current upswing and with it the chances of implementing Lisbon.

For achieving the Lisbon strategy will benefit every Member State. The principle underpinning the European Union is well-established: Europeans better hang together or they will hang separately. The single market in goods and services promotes trade that benefits every Member State. The euro creates a monetary union of predictable, stable low interest rates and low inflation that benefits every Member State. No single European country can achieve an improved environment just by itself; and the better the European economy performs as a single economy, the more inward investment flows to every Member State to take advantage of the improved general European business climate. In the same way, the effects of building a European knowledge economy spill over to benefit all.

Lisbon is a strategy that is best pursued collectively by all Europe if the maximum benefits are to be yielded. In order to ensure the benefits, Member States must take their responsibility and take ownership of the process. The European Commission must be prepared to name and blame those that fail as well as “fame” those that succeed. Too much is at stake to respect the sensibilities of those who hinder the pursuit of the common European good. And the EU’s common policies, including its budgets, must reflect the Lisbon priorities. If Europe is to achieve its goals it must act single-mindedly and with focus; and it must act now.

# Chapter Two
# Unblocking the blockages: releasing the potential

### What to do?

There is no single magic bullet that will deliver the higher growth and jobs that Europe urgently needs. Rather there are a series of interconnected initiatives and structural changes that through their cumulative reinforcement by simultaneous implementation in every Member State will provide both the comprehensiveness and force to release the undoubted potential that exists in the European economy. Each element of the Lisbon strategy contributes to the success of the whole.

Necessarily Member States start from differing positions. This requires an interpretation of the Lisbon's goals within individual national contexts and challenges rather than as a blanket injunction to improve every economic indicator regardless of individual national positions – otherwise the strategy will make no sense to public opinion in individual Member States.

However there are five broad priority areas of policy where the European Union and individual Member States need to ensure making progress both to help ensure its own economic dynamism and the vigour of the whole European economy from which each Member State benefits. The realisation of the knowledge society, the completion of the single market and promotion of competition, including services and financial services, the establishment of a favourable climate to business and enterprise, building an adaptable and inclusive labour market and the vigorous promotion of win/win environmental economic strategies are together sources of economic growth and higher productivity. And all, in the view of the High Level Group, is more likely to take place against a background of growth supporting macro-economic policies.

Perhaps individual Member States can boast achievement in one or even two of these policy priority areas. None can boast success in all five, which is what is required if Lisbon's ambition – after all no more than giving Europe's citizens the opportunity and quality of life they want – is to be achieved. The task is to convince Europe's leaders and publics intellectually of Lisbon's case; to develop policies in each Member State, supported by an appropriate European wide framework, that address particular member state's circumstances and then to act in a more determined way than we have so far witnessed.

In conclusion to restate; it is not the pursuit of any one of these objectives that will raise Europe's productivity and growth, but all of them – obviously tailored to the particular position of national economies. And the more buoyant the wider economy, the easier it will be to introduce difficult reforms. The rest of this chapter contains specific recommendations, with which government leaders can show their commitment to a strategy for growth and employment.

## 1. REALISING THE KNOWLEDGE SOCIETY

***The Lisbon Strategy calls for:***

***Information society****: defining a regulatory framework for electronic communications; encouraging the spread of ICTs; creating conditions for e-commerce; supporting European leadership in mobile communications technologies.*

***Research:*** *setting up of an area of research and innovation; boosting spending on R&D to 3% of GDP; making Europe more attractive for its best brains; promoting new technologies.*

***Education and human capital:*** *halving the number of early school leavers; adapting education and training systems for the knowledge society; fostering lifelong learning for all; promoting and facilitating mobility.*



### Why the Knowledge Society?

The Lisbon European Council rightly recognised that Europe's future economic development would depend on its ability to create and grow high value, innovative and research-based sectors capable of competing with the best in the world.

The evidence that the higher research and development expenditure, the higher subsequent productivity growth, is overwhelming. Although it may seem repetitive and even platitudinous one of the preconditions for any increase in European productivity growth is to raise R&D spending. Studies demonstrate that up to 40% of labour productivity growth is generated by R&D spending and that there are powerful spill-over effects into other economies; of course attention needs to be paid to the way in which the money is spent. One of the most disappointing aspects of the Lisbon strategy to date is the importance of R&D remains so little understood and so little progress has been made.

The knowledge society is a larger concept than just an increased commitment to R&D. It comprehends every aspect of the contemporary economy where knowledge is at the heart of value added – from high-tech manufacturing and ICT through knowledge intensive services to the overtly creative industries such as the media and architecture. Up to 30% of the working population are estimated in future to work directly in the production and diffusion of knowledge in the manufacturing, service, financial and creative industries alike. A large proportion of the rest of the workforce will need to be no less agile and knowledge based if it is to exploit the new trends. Europe can thus build on its already useful commitment to education and training and generally strong commitment to investment to create a knowledge society along with "knowledge-in-the-society", to win potential world leadership.

In particular is ICT opening up the possibility of a fundamental re-engineering of business processes and wider economic structures to create the network economy and society. It permits every step in value generation to become smarter; value is being created less in the simple transformation of inputs into outputs but more in enlisting the new capacity and competencies created by ICT fundamentally to meet individualised and complex customer needs – whether business to business relationships or business to consumer.

Successful companies are becoming more networked, customer focused and agile in which an ethic of demand oriented service rather than producer oriented production is conferring market share and value generation alike. Indeed more and more value generation lies in distribution, financing, marketing and service rather than manufacturing the original product – important though that remains. Knowledge and the potential of ICT penetrate every link in the economic chain, not just the manufacturing core.

However neither Europe's knowledge society in general nor its ICT sector in particular are as strong as they need to be to achieve this vision. Whether patent applications, numbers of scientific researchers, universities standing in international rankings, numbers of Nobel Prize winner or references in scientific papers Europe trails the US. The opportunity to create global standards is insufficiently seized. The European IT sector represents 6% of European GDP compared with 7.3% in the US[6], while European investment in IT capital goods has consistently lagged behind the US by around 1.6% of GDP in the recent past[7].

There are some strengths too. Europe produces nearly twice as many science and engineering graduates as the US. There are individual sectors, such as civil aerospace, mobile phones and power engineering where Europe is strong. Too much of US technological advantage is concentrated in defence and defence related sectors. Europe has a solid base; what is now required is a recognition of the importance of the knowledge society to Europe's future and a determination to build it.



***Attracting and retaining world-class researchers***

Too many young scientists continue to leave Europe on graduating, notably for the US; too few of the brightest and best from elsewhere in the world choose to live and work in Europe. Therefore needs Europe to dramatically improve its attractiveness to researchers.

European researchers continue to face administrative obstacles to mobility within the EU, related to social security entitlements and the recognition of qualifications. These problems must be resolved; further developing a system of mutual validation of national quality assurance and accreditation processes would be an important step in the right direction. More also needs to be done to facilitate the entry of researchers and their dependants from third countries through simplified, fast-track work-permit and visa procedures.

However, there are also financial questions requiring attention. Member States need to urgently address the problem of funding for universities. If Europe wants to attract more of the world's best researchers, the question of improving their research environment and remuneration needs to be addressed now.

Creative interaction between universities, scientists and researchers on the one hand and industry and commerce on the other that drive technology transfer and innovation are necessarily rooted in the close physical location of universities and companies. There is already ample evidence around the world that high-tech clusters are built on this interaction, but ideopolises – for example Helsinki, Munich and Cambridge – go further. They have an array of other supporting factors – notably a sophisticated communications and transport infrastructure; financial institutions willing to provide the necessary risk capital to

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[6] The Economic Future of Europe, Olivier Blanchard, Working Paper 04-04, MIT

[7] Between 1995 and 2001 investment in IT capital goods ran at 1.6% of GDP less than the US, Franceso Daveri, Why is There a Productivity Problem in the EU? Centre for European Policy Studies

entrepreneurs and specialists in technology transfer; supportive public authorities that facilitate the network structures driving creative interaction; and are attractive environments for knowledge workers. Ideopolises are emerging as the cities at the heart of dynamic, high growth knowledge based regions.

**Key recommendation**

*The EU needs to attract more of the best and brightest researchers in the world through raising its attractiveness. Therefore the 2005 Spring European Council should agree on an action plan to reduce the administrative obstacles for moving to and within the EU for world-class scientists and researchers and their dependants. This action plan, to be implemented by Spring 2006, should address all of the principal administrative obstacles existing in Member States, which discourage researchers from moving within and to the EU.*
*Fast-track work-permit and visa procedures should be introduced for researchers and the mutual recognition of professional qualifications must be improved.*

### *Making R&D an top-priority*

There is overwhelming evidence of the vital importance of boosting R&D as a prerequisite for Europe to become more competitive. To fail to act on that evidence would be a fundamental strategic error – yet many Member States remain worryingly complacent and a strong need to instil a much greater sense of urgency.

Major structural obstacles still lie in the way of higher levels of R&D spending, both private and public. Tax incentives for newly founded small and medium size enterprises (SME's) that invest in research should be encouraged. Public support for R&D at the EU and national levels should be boosted, both to strengthen the science base and increase the leverage effect on R&D investment by the private sector. Public-private partnerships should be facilitated and encouraged as a means of boosting investment; Europe's science base should be strengthened by funding and co-ordinating long term basic research ranked by scientific merit via the creation of a European Research Council. At the same time, Member States and the Commission should look at ways in which public procurement could be used to provide a pioneer market for new research and innovation-intensive products and services.

**Key recommendation**

*To foster scientific excellence, the European Parliament and the Council should agree by the end of 2005 (within the scope of the 7th framework programme) on the establishment of an autonomous European Research Council (ERC) to fund and co-ordinate long term basic research at European level.*

In addition, increased efforts should be mobilised at national and EU level by all concerned stakeholders to promote technological initiatives based on Europe-wide public-private partnerships.

*Reaping the full benefits of ICT*

In order to ensure future economic growth, the EU needs a comprehensive and holistic strategy to spur on the growth of the ICT sector and the diffusion of ICTs in all parts of the economy. The top priority of this strategy should be to ensure that the regulatory framework for electronic communications that was adopted in 2002 is fully implemented and strictly enforced, so that competition is more effective in driving down prices for consumers and businesses. This demands closer co-operation between the European Commission, national competition authorities and national regulatory authorities.

This strategy must also focus on boosting by 2010 the accessibility to broadband of 50%, take-up of which remains slow and patchy in too many Member States. More must be done to bring down access prices, provide new content to stimulate demand and accelerate the rollout of broadband networks, especially in rural areas. Efforts should focus not only on fixed broadband networks but also on wireless networks (3G and satellites). The latter offers a cost-effective high-speed Internet access to bridge the digital divide and thus contribute to the objectives of social and regional cohesion.

Furthermore, Europe needs a regulatory framework that stimulates the development of standards that can drive the development and diffusion of new technologies within and outside the EU.



*Protecting intellectual property to promote innovation*

Companies will only invest in innovation if they have the certainty that they will be able to reap the rewards of that investment. An essential prerequisite for this is a legal framework for the protection of intellectual property rights that is accessible at low cost to Europe's SMEs and academic institutions – something which is manifestly not the case at present. Most urgently, the EU should adopt the pending proposal on the Patenting of Computer-Implemented Inventions; and of course, the Community Patent.

***Key recommendation***

*On the Community Patent, the time has come for the Council to adopt it or drop it. Agreement should be reached on this fundamentally important piece of legislation before or at the 2005 Spring European Council. The agreement must ensure that the Community Patent really does reduce the complexity, time and costs of protecting intellectual property. This is why the High Level Group appeals to the European Council to overcome the outstanding language issue.*

## 2. KEEPING OUR COMMITMENTS TO THE INTERNAL MARKET

***The Lisbon Strategy calls for:***

***Ensuring effective transposition of EC Law:*** *accelerating transposition of EC legislation (98.5%).*

***Removing obstacles to the free movement of services in the EU.***

***Completing the Internal Market for network industries:*** *progressively liberalising markets and network industries, notably gas and electricity (2007); postal services (2006); rail transport (2008); and airspace.*

***Completing the Internal Market for financial services*** *(2005).*

***Ensuring fair and uniform application of competition and state aid rules:*** *reducing state aid to 1% of GDP; defining the new mergers regime and take-over bid rules; and updating public procurement rules.*

**Why the Internal Market?**

Facilitating free movement of persons, goods, services and capital in an area without internal frontiers is a crucial mechanism that generates economic growth. The internal market permits those companies and sectors that have relative competitive strengths to build on their specialist advantages and grow, and this becomes a self-reinforcing trend. Resources are used by those most capable of using them, who in turn can build up economies of scale so lowering costs and prices; there is a general uplift in real incomes, profits and innovation. Durable economic growth has always been associated with market opening and strong growth in trade.

Europe's internal market has worked to support this twin interaction of growth in trade and national economies. Separating out the effects of the internal market from other factors is difficult, but the European Commission estimates[8] that after 10 years of the internal market European GDP is 1.8% higher than it would have otherwise been and 2.5 million more jobs have been created. This contribution amounts almost to 10% of the EU potential growth-rate on an annual basis.

But the effects are weakening as attempts to complete the internal market in goods and create one in services have stalled. Intra-EU trade in manufactured goods has been shrinking since 2001, and it's the same story in services. Another indicator of the incomplete internal market is that prices vary so widely across the EU – price convergence is a long way short of US levels[9]. At the same time, the EU has become less attractive as a place to invest. Foreign investors continue to invest in the EU, but more leaves the EU than comes in. Better market integration would make the EU more attractive to potential investors from inside the Union and from third countries.

Continuing to open Europe's markets in goods and services, and conversely resisting protectionist pressures, are thus fundamental to Europe's growth prospects – but the internal market programme is felt to be yesterday's business and does not receive the priority it should. It is a fatal policy error. There is enormous scope for further market integration and greater economic gains for both consumers and enterprises. Along with investment in R&D, completing the internal market is the readiest way to boost productivity and innovation.



8 SEC [2002] 1417, 'The Internal Market – Ten years without frontiers'

9 The Internal Market Scoreboard shows EU price divergences in groceries as 80% higher than in the US, with an even bigger difference for transport services. Price convergence is a good indicator of market integration.

### *A commitment to faster transposition*

One of the most persistent obstacles is the failure of too many Member States to enact the commitments they make in the Council within the agreed time limit. There is little benefit in governments agreeing to measures in Brussels if they do not then show the same commitment when it comes to implementing those measures at national level. In spite of the European Council's repeated calls for zero tolerance for excessive delays in transposition, this remains a huge problem. Furthermore, in too many cases, implementing legislation is not in line with the original Directive or is excessively complex, negating the benefits intended to stem from a single set of rules and often placing unnecessary burdens on business. In both cases, the repeat offenders know who they are.

> ***Key recommendations***
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> *Every Directive that is late in being implemented by a Member State reduces the competitiveness of the entire Union; there is no excuse for this and it must no longer be tolerated*
>
> *- At the beginning of 2005, the Commission should produce a full list of Internal Market legislation still awaiting transposition in each of the 25 Member States, to be annexed to the Spring European Council conclusions. This list should be sorted by Member State, beginning with the worst offender.*
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> *- In the light of this scoreboard, the 2005 Spring European Council should set a final deadline by which transposition should be completed.*

### *Removing obstacles to the free movement of services*

Opening up the many blockages is crucial, and not only in the market for goods. Europe's services sector accounts for 70% of economic activity in the EU; most of new jobs between 1997 and 2002 were generated in the services sector. Yet services only account for 20% of Europe's trade, largely because of a wide range of legal and administrative barriers. One of the great prizes of European integration and major boosts to growth and employment would be the creation of a single market in services.

Requiring urgent attention and decisive resolution is the lack of competition in the services sector, which has been the principal driver of growth and employment in the past decade and will continue to be in years to come. Regulatory obstacles to service providers mean that in a swathe of areas, Europe remains fragmented into separate national markets – many of which are effectively closed for business to potential competitors based elsewhere in what should be a single market. The result is higher prices for consumers, lower productivity growth and levels of intra-EU trade in services that are lower than they were a decade ago[10]. This situation has to change and it has to change now, bearing in mind that special attention should be paid to concerns in society. Clearly, it would be inconsistent with the Lisbon model to achieve competitiveness gains at the price of social dumping.

[10] COM [2003] 238, p. 10.

***Key recommendation***

*The European Parliament and the Council should agree on legislation to remove obstacles to the free movement of services by the end of 2005. There must then be a clear commitment on the part of Member States to ensure that national rules are not used as an excuse to hinder or block service providers based in other Member States; the Commission should treat the enforcement of this requirement as a priority.*

***Identifying and removing barriers to competition***

Even in supposedly liberalised sectors such as network utilities, incumbent operators continue to dominate national markets, often limiting the advantages to consumers. In order to foster further liberalisation and opening more sectors to EU-wide competition the European Commission should carry out sector-wide enquiries to identify barriers to competition. This should ensure that not only on paper but also in practice effective competition exists, especially where local rules have the effect of preventing competitors from entering into the national market.

The impact of regulation on competition and ultimately on consumers should be systematically reviewed so as to ensure that regulation would not unnecessarily impede economic activity. In close co-operation with national competition and regulatory authorities, the Commission should subsequently find effective and innovative means of removing these barriers. In the first instance, attention should focus on high-value-added sectors and network utilities, which are vital to the health of the European economy. This will assist in creating an environment where the most competitive companies reap the rewards of innovation and efficiency, driving down prices and increasing consumer choice.

In the energy sector, new legislation providing clear liberalisation targets in electricity and gas markets has been put in place. Member States are required to open the electricity and gas markets for all non-household customers by July 2004, and for all customers by July 2007. It is crucial that all Member States comply fully with this obligation. Ensuring a true level playing field in the electricity and gas sectors will allow eco-efficient innovations to be taken up in these newly liberalised markets and encourage investments by new entrants.

***Making the free movement of goods a reality for all***

A range of obstacles also continues to exist to the free movement of goods – obstacles that must no longer be tolerated. Free movement continues to be hindered by a range of local rules, often applied arbitrarily and in clear contradiction to the mutual recognition principle that is the cornerstone of the Internal Market. Furthermore, even in areas where technical rules have been harmonised, like construction materials or machinery, the slow development of technical standards has meant that obstacles have remained in place much longer than necessary. The Commission must dedicate appropriate resources to identifying and pursuing infringements by the Member States in this area. It should use its synthesis report to inform the Spring European Council each year of ongoing obstacles to the free movement of goods in each Member State and treat the removal of these obstacles as a top political priority. This is worthwhile as the estimated cost of the non application of the mutual recognition principle is around 150 billion Euro's.

### *Unleashing the dynamism of financial markets*

Dynamic and highly competitive financial markets are not only desirable in themselves – they are an essential driver of growth in all other sectors of the economy and must be a cornerstone of efforts to boost the EU's economic performance. To deliver significantly lower costs to business and consumers, a Financial Services Action Plan (FSAP) was presented in 1999 as a package of legislative and non-legislative measures to create a single EU market for wholesale financial services, to create and open retail markets and to put in place prudential rules and supervision.

This FSAP – to be fully implemented by 2005 - should be supplemented by measures to reduce barriers to cross-country clearing and settling and to facilitate the integration of retail financial markets, in particular by reducing restrictions to more flexible mortgage financing in a number of Member States. Moreover, a successful integration of financial services market requires enhanced convergence also in the supervisory practices. At present, the coexistence of too many regulatory supervisors in Europe is not conducive to such convergence. However, in the context of the FSAP, a process of enhanced co-ordination between national supervisors has started. The High Level Group calls upon the Commission to assess progress of supervisory practices in financial services. This assessment should be presented to the European Council in Spring 2006 and should, if necessary, include proposals to speed up the process of convergence.

Clearing and settlement of transactions is the backbone of the financial system. While national arrangements for this are generally efficient, they combine inefficiently at the EU level. Accordingly, a cross-border transaction is unnecessarily complex and can cost many times more than the corresponding services for a domestic transaction. In order to facilitate cross-border trade in securities, integrated and efficient clearing and settlement arrangements at the EU level are required. In turn these would deliver a powerful impetus to the process of financial integration.

Facilitating the integration of retail financial markets is a natural follow-up to the FSAP to ensure lower costs, greater efficiency, more access to credit on more competitive terms and more consumer friendliness - and also to help SMEs have better access to finance. In particular, reducing restrictions on refinancing mortgage debt and offering improved possibilities to finance a larger proportion of the purchase price of property via more generous and cheaper mortgage loans could extend home ownership and also boost consumption. Transaction costs on housing are too high in most Member States. More flexible housing markets would encourage labour mobility, the development and efficiency of the financial services sector, empower home-buyers and support more consumer spending.

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| ***Key recommendations*** |
| *The Council should adopt remaining legislation of FSAP before Spring 2005. Member States should, before end of 2005, transpose the relevant FSAP measures into national law.* |

*The Commission should draw up a strategy for reducing barriers to cross-border clearing and settlement before Spring 2005 European Council.*

*The Commission should, before end of 2005, present an analysis and suggestions for action to facilitate integration of retail financial markets.*

***Cutting tax compliance costs for companies***

In parallel with the integration of financial markets, there is also a need for measures to be taken in the area of company and tax law, to address obstacles to businesses organising themselves effectively on a pan-European scale. The harmonisation of the corporate tax base throughout the Union would significantly cut the administrative burden on companies operating in several Member States and should be agreed without delay. Similar measures specifically designed to reduce the tax compliance costs faced by SMEs should also be adopted, notably the introduction of a one-stop shop for companies to deal with their EU-wide VAT obligations.



***World-class infrastructures for the world's largest Internal Market***

Europe's level playing field remains cluttered with infrastructural obstacles. For too many companies accessing areas of the Internal Market on the other side of the continent is effectively impossible. For others, the non-availability of broadband, either at accessible prices or at all, is an equally significant structural disadvantage compared to competitors elsewhere.

More urgently than ever in the light of enlargement, Europe's Internal Market needs to be connected. Many of the new Member States are not only on the periphery of the Internal Market geographically; they are also in desperate need of expanded and modernised infrastructures. There needs to be more targeted investment in infrastructure coupled with more effective competition in areas like electronic communications, energy and transport to drive down costs for businesses wherever they are located. The Quick Start Programme for priority infrastructural projects, agreed by the European Council in December 2003, should be implemented without further delay.

## 3. CREATING THE RIGHT CLIMATE FOR ENTREPRENEURS

***The Lisbon Strategy calls for:***

***Regulatory climate conducive to investment, innovation and entrepreneurship:*** *facilitate access to low-cost finance, improve bankruptcy legislation, take into account SMEs' specificities (2000), improve the industrial framework, encourage responsible corporate governance.*

***Lower costs on doing business and remove red-tape:*** *develop a better regulation strategy at both European and national level (2001), reduce time and costs for setting up a company.*

**Why create the right climate for entrepreneurs?**

Increased knowledge and an open internal market do not automatically drive innovation, competitiveness and growth. It requires entrepreneurship to design new products and services and take advantage of market opportunities to create value for customers.

Increasingly, new firms and SME's are the major sources of growth and new jobs. Entrepreneurship is thus a vocation of fundamental importance, but Europe is not 'entrepreneur-minded' enough. It is not attractive enough as a place in which to do business. There are too many obstacles for entrepreneurs and therefore Europe misses many opportunities for growth and employment. Much can and must be done to improve the climate for business.



***Improving the quality of legislation***

A first obstacle for entrepreneurs is the overall burden of rules and regulations imposed on businesses. Although regulation is often launched with the best of intentions, there is now a growing feeling that a tipping point has been reached in which gains from incremental regulation is outweighed by the costs – especially among manufacturers. There needs to be a gear change. The present situation leaves insufficient room for risk taking and demands too much attention and resources from the entrepreneur. Removing this obstacle calls for less regulation, but even more importantly better and smarter regulation. Legislation of poor quality or which requires an excessive accumulation of administrative provisions to implement damages competitiveness.

A balance must be struck between regulation and competition. Without for example contract-law not many transactions would take place. Thus, it is clear that across the board deregulation is not the answer: many regulations aim to increase confidence of entrepreneurs and customers alike, and can be a source of competitive advantage. It is necessary for decision-makers to be well-informed about the consequences of their decisions on competitiveness. The High Level Group, therefore, believes that greater attention must be given to ensuring that evaluations of key legislative measures are conducted prior to final adoption.

Thus, the European Parliament, the Council and the European Commission agreed on an 'Inter-institutional Agreement' on 'Better Lawmaking' in 2002. The Commission committed to improving the quality of legislative proposals, as well as stakeholder consultation with all interested parties and the conducting of extended socio-economic and environmental impact assessment of proposed measures. Both European Parliament and Council recognised that the process of amending legislation influences its quality and therefore committed to assess the impact of any substantive amendments. Moreover, the initiative Ireland, the Netherlands, Luxembourg and the United Kingdom took, stresses the need to reduce the administrative burden on businesses.

***Key recommendation***

*The European Commission should continue to develop its instrument for analysing the impact of legislative proposals so that the objectives of competitiveness and sustainable development are incorporated more effectively.*

*The Commission and the Member States should agree on a common definition of administrative burden before or at the Spring Council 2005. The Commission must assess the cumulative administrative burden on companies and set a target for reducing this burden. Similarly must the Member States undertake an analysis of their national law and set themselves a target for reducing the national administrative burden. Both Commission and Member States should indicate before July 2005 by how much and by when they are going to reduce the administrative burden in key priority sectors.*



In reducing administrative burdens, Commission and Member States must give special attention to regulations that have an impact on the start-up of businesses. Although much progress has been achieved in some Member States, the time, effort and costs required for setting up a company must be further reduced. There is scope for improvement regarding multiple procedures, contact and information points, forms, licences and permits needed and costs.

***Key Recommendation***

*Member States must reduce drastically the time, effort and cost of setting up a business by end of 2005. The objective should be to converge towards the average performance of the current best three Member States. The introduction of a one-stop shop for setting up a business is highly recommended.*

**Increasing the availability of risk-capital**

The limited availability of finance is a second obstacle for setting up and developing businesses in Europe. Company financing in Europe is currently too much lending based and not enough capital risk-based. This makes it especially hard for start-ups and SME's to attract sufficient financing, as they cannot meet the demands for guarantees by traditional financial institutions.

It is safe to say that the environment for risk capital investments still needs to be improved. Investors in Europe should be more encouraged to commit to long-term involvement in start-ups. In spite of the Risk Capital Action Plan and the progress made in other initiatives, important differences between Member States persist and risk capital investment levels in the US are still double than those in the EU. There is insufficient mobilisation of capital, but also the infrastructure to channel more capital to investment opportunities is underdeveloped.

Equity markets and funds remain fragmented and below their critical size. As a consequence the risk run by funds and private investors is unnecessarily increased as exit strategies are blocked. In turn this does lead to lower investments and Europe missing out on many opportunities. Therefore the whole chain of creating worthwhile opportunities and assuring investment in them needs to be reinforced, thus linking funds, companies, industry and universities.

Financial and public institutions offering different financing instruments supporting a specific policy objective, such as privileged loans, grants or subsidies could co-operate better to make it easier for companies to locate the appropriate funding and to make use of the opportunities offered. The involvement and expertise of the European Investment Bank could be used more systematically. The Commission's analysis on deepening the access to capital markets, as asked for by the High Level Group, should provide other concrete answers on the appropriate measures to mobilise the required risk-capital. What is abundantly clear is that the stimulation of networking, including in the clusters and ideopolises discussed earlier, is crucial and requires attention from policy makers.

A third obstacle is that entrepreneurs are too often stigmatised when they fail. Entrepreneurial activity implies by definition taking the risk to fail. Despite evidence that failed entrepreneurs learn from their mistakes and perform better in their next business, customers and financiers are reticent to place orders. Honest bankruptcy still carries too many severe legal and social consequences. If more entrepreneurial initiative is to be promoted, a radical shift is required.

When the above obstacles are addressed determinedly, Europe can begin to expect to unlock its entrepreneurial potential and offer its citizens new opportunity to develop themselves. However, a one-off effort will not suffice: long term trust in the stability of the framework will need to be established for real growth to occur.



## 4. BUILDING AN ADAPTABLE LABOUR MARKET FOR STRONGER SOCIAL COHESION

***The Lisbon Strategy calls for:***

***Increasing employment rate:*** *67% (by 2005) and 70% (by 2010) for total employment rate, 57% (by 2005) and 60% (by 2010) for women employment rate, 50% for older workers by 2010. Progressive increase of about 5 years in the effective average age at which people stop working.*

***Defining a multi-annual programme*** *on adaptability of businesses, collective bargaining, wage moderation, improved productivity, lifelong learning, new technologies and the flexible organisation of work by the end of 2002.*

***Removing disincentives for female labour force participation,*** *further equal opportunities.*

***Adapting the European social model to the transformation to the knowledge economy and society:*** *facilitate social security in cross-border movement of citizens, adopt temporary agency work directive (2003), ensure sustainability of pensions schemes, introduction of the open method of coordination in the field of social protection.*

***Eradicating poverty:*** *agreement on a social inclusion programme (2001), mainstream the promotion of inclusion in national and European policies, address specific targets groups issues.*

### Why build an inclusive labour market?

Employment is the best way for people to develop themselves, make a contribution to society and avoid poverty. It is essential for achieving greater social cohesion within the European

Union. Furthermore, having more people in employment is the best way of guaranteeing the social and financial sustainability and further development of European welfare systems.

Demographic ageing and globalisation will have increasing consequences on the sustainability of our social model and specifically on our labour markets. To achieve stronger and more sustainable growth, Europe – in other words its Member States - must face those challenges. Increasing the level of employment requires providing people and companies with the tools and opportunities to exploit these changing conditions positively.

The call for more reform is too frequently seen as no more than code for more flexibility which in turn is seen as code for weakening worker rights and protections; this is wrong. The High Level Group understands that flexibility is about agility, adaptability and employability for which the key is the ability for workers constantly to acquire and renew skills, and for a combination of active labour market policies, training and social support to make moving from job to job as easy as possible. Nor should reform mean that the social dialogue is taken out of the heart of Europe’s labour market. It is essential to its productivity and ability to adapt to change.

Modern and efficient social protection systems make an important contribution to Europe's sustainable growth and are crucial for the financial viability of the European social model. Social inclusion policies are not only important to combat poverty, but also contribute to increasing labour supply. Reforms to ensure safe and sustainable pension systems should aim at providing the right incentives, both for workers to stay active longer and for employers to hire and keep older workers on the payroll. Health care systems play a key role, not only in combating disease and risk of poverty but also in generating social cohesion, a productive workforce, employment and hence economic growth.

European growth depends also on more people in the labour market, even though ageing makes the working population decline. To deliver this strategic objective, Europe needs to invest in a high-skill labour force, to recommit to labour market reforms and to accommodate demographic changes. Europe’s labour markets and employment policies are more efficient and adaptable thanks to reforms in many Member States in recent years. Strong employment growth in the late 1990s and the noticeable resilience to economic downturns are encouraging signs of progress. Compared with four years earlier, over 6 million people more were employed in 2003 and unemployment and long-term unemployment were significantly lower (by 30% and 40% respectively). This is convincing proof that reforms were necessary and that they do pay off.

In order to make work a real option for all, more needs to be done to increase the participation of women. This calls for the removal of remaining tax disincentives to work, determined action to address the roots of the gender pay gap and the stricter enforcement of non-discrimination legislation. The better reconciliation of family and working life also demands the provision of availability, affordability and good quality of childcare and eldercare.

An in-depth examination of the European labour markets has been carried out by the European Employment Taskforce in 2003. Concrete options and recommendations have been presented to Member States, institutions and stakeholders. All of them should now engage themselves in the concrete implementation of key priorities to improve European employment performance and the financial and social sustainability of the social model.

**Key recommendation**

*Member States in close consultation with social partners should report on the implementation of the recommendations they endorsed in March 2004, including their employment performance and sustainability of social systems, so that the 2005 Spring Council can assess the progress made. In this respect, the Social Affairs Council should prepare and co-ordinate this assessment.*

***More effective investment in human capital***

The productivity and competitiveness of Europe's economy are directly dependent on building a well-educated, skilled and adaptable workforce that is able to embrace change.

This is why it is necessary to devise ambitious policies to raise educational levels, notably by halving the number of early school leavers in Europe, ensure greater participation in training throughout working lives and make lifelong learning a reality. All actors – public authorities, individuals and businesses – must accept their share of the responsibility for raising the levels and efficiency of investment in human capital. Incentives are needed to boost investment in training within individual companies and across sectors, in order to support employers to provide suitable access to learning.

**Key recommendation**

*Members States in close co-operation with social partners should adopt national strategies for life long learning by 2005, in order to address the current climate of rapid economic restructuring, to raise labour market participation, to reduce unemployment and to enable people to work longer.*



***Increasing the adaptability of workers and enterprises***

Better responsiveness of European economies to anticipate, absorb and change and a high degree of adaptability in the labour market is in the interest of the whole society. The creation of new businesses and greater adaptability of workers and companies must be fostered and job creation maximised.

The challenge for the labour market is to find the balance between flexibility and security. Finding this balance is a shared responsibility between employees and employers and social partners and governments. Those involved should work together to enable people to stay in employment by making sure that people possess needed and up-to-date skills and create structures in which they can best combine their work and non work responsibilities. The task is to foster new forms of security, moving away from the restrictive paradigm of preserving jobs for life to a new paradigm in which the objective is to build people's ability to remain and progress in the labour market.

If Europe is to compete in the global knowledge society, it must also invest more in its most precious asset - its people. Yet at present, far from enough is being done in Europe to equip people with the tools they need to adapt to an evolving labour market, and this applies to high and low-skilled positions and to both manufacturing and services. Nor is anything like enough being done to attract and retain the best scientific brains in the world.

To equip Europe with the highly-educated, creative and mobile workforce it needs, education and training systems must be improved so that enough young people are graduating with the appropriate skills to obtain jobs in dynamic, high-value and niche sectors. Member States must make lifelong learning schemes available to all - and all must be encouraged to take part in them. The potentially devastating consequences of the ageing population mean that boosting participation of older workers in the labour market is of fundamental importance. Therefore lifelong learning is not a luxury, it is a necessity – for if older people are to be able to remain active, they need to be equipped with skills that match the requirements of the knowledge society.



***Dealing with ageing***

Finally, to underpin economic growth, Member States must attract more people in employment and ensure that they can achieve sustainable integration in jobs. In this respect, it is essential to increase employment by active labour markets policies, and try to prevent, remove or reduce low pay traps through adequate reforms of tax and benefits systems.

In the light of the approaching decline of the working age population, elder workers are key. The employment rate target for workers aged 50 and over (50% by 2010) will be missed unless far-reaching measures are urgently taken, notably by developing lifelong learning, improved health and working conditions

> ***Key recommendation***
>
> *Member States should develop comprehensive active ageing strategy by 2006. An active ageing strategy requires a radical policy and culture shift away from early retirement, towards three key lines for action: providing the right legal and financial incentives for workers to work longer and for employers to hire and keep older workers; increasing participation in lifelong learning for all ages, especially for the low-skilled and for older workers; and improving working conditions and quality in work.*

Mobility throughout the Union should also be strengthened to allow workers to benefit from new opportunities. In this context, Member States should seriously evaluate the impact of the restrictions on labour movement from the new Member States as foreseen in the transition periods. On that basis, they should also assess whether they are still needed.

Finally, demographic ageing in the years and decades to come calls for proactive analysis and policies on ways and means to satisfy future labour market needs. Even if full use is made of the labour market potential, "selective" non-EU immigration will be needed, to meet European labour market shortages and partly to offset the negative consequences of the "brain drain". It would be wise for Member States to prepare themselves timely and thoroughly for this decision because experience shows that the successful inclusion of migrants and ethnic minorities in society, and especially in the labour market, demands considerable and sustained effort.

## 5. Working towards an environmentally sustainable future

***Lisbon strategy calls for:***

***Climate change**: rapidly ratify the Kyoto Protocol (2002), show progress in delivering Kyoto targets (by 2005), meet target of 12% of primary energy needs and 21% of gross electricity consumption form renewable energy sources.*

***Decoupling economic growth from resource use**: tackle rising volumes of traffic, congestion, noise and pollution with full internalisation of social and environmental costs, develop a Community framework for pricing of transport infrastructure (eurovignette), ensure a sustainable use of natural resources and level of waste.*

***Definition of a new regulatory framework**: adoptions of the energy taxation directive (2002), environmental liability (2004), 6th Environmental Action Programme.*



### Why the environment is a source of competitive advantage for Europe?

Well thought-out environmental policies provide opportunities for innovation, create new markets, and increase competitiveness through greater resource efficiency and new investment opportunities. In this sense environment policies can help achieve the core Lisbon strategy objectives of getting more growth and jobs.

Moreover, the case for reinforcing integration of environmental considerations into the strategy is strengthened by the need to seriously address the existing pressures on the environment in order to avoid damage to health, biodiversity, property, and economic activity, now and in the future. Failure to act now means greater, and possibly irreversible, damage or higher remedial costs in the long term.

As recalled earlier, the Lisbon strategy reflects Europe's commitment to embed respect for the environment in the core of the growth and jobs generation process so it is part of Europe's competitive advantage. Indeed taking care of the environment should remain an important dimension of the strategy as it can both constitute a source of competitive advantage in global markets and increase competitiveness. But this virtuous combination of environmental aspects and enhanced competitiveness is not automatic; it requires the right choice of policy instruments and the need for governments to carefully strike the balance between environmental, social and economic impacts, both in the short and the long-term.

### *Environment and competitiveness: exploiting win-win opportunities*

Europe can gain a first mover advantage by focusing on resource efficient technologies that other countries will eventually need to adopt. European companies are already world leaders in some clean products and processes and this gives them an advantage in emerging markets where rapid economic growth is placing increasing pressure on their environments.

For example in China at present only three in every thousand person owns a car, but as wealth increases China has the potential to become the world's largest car market. At the same time, given the magnitude of air pollution problems and of the oil demand growth, the Chinese government is seeking to catch up with European vehicle emissions standards by 2010. This, and the relatively low incomes in China, will steer consumers towards cleaner and more fuel efficient vehicles. EU manufacturers are well placed to meet this demand[11].

Promoting eco-efficient innovations is clearly a win-win opportunity that should be fully exploited in view of reaching the Lisbon goals. Innovations - that lead to less pollution, less resource-intensive products and more efficiently managed resources - offer both growth and employment while at the same time offering opportunities to decouple economic growth from resource use and pollution. There are many examples of these eco-efficient innovations ranging from electronics to agriculture and including energy, transport, chemicals or healthcare sectors. The Environmental Technology Action Plan aims to promote the development and use of these technologies. It has identified several market barriers, which need to be overcome if Europe is to fully tap the potential of eco-efficient innovations.

Firstly, promotion is needed of eco-efficient innovations in major investment decisions, notably in energy and transport. Establishing an appropriate regulatory framework to allow eco-innovations to be taken up in markets is essential. Nowadays prices are distorted in some markets, leading to a misallocation of resources and creating disincentives for investors and buyers to participate. Market prices need to reflect the real costs of different goods and services to society. This requires removing gradually environmental harmful subsidies and including progressively externalities in prices, taking account of other policy objectives such as competitiveness in the global economy and social aspects.

Secondly, even more pressing for companies, which are active in the field of eco-innovations, is the limited access to finance. At present investments in eco-efficient innovations have longer payback times and therefore involve greater risks for investors. The Netherlands offers an example of how Member States can achieve this. The Netherlands promotes green investment funds, managed by commercial banks, through granting tax reductions to private individuals investing in such a fund. This increases the available capital for companies, which are active in this market.



***Key recommendation***

*The Commission, Council and Member States should promote the development and diffusion of eco-innovations and build on existing European leadership in key eco-industry markets.*

*The Commission should report on overall progress of the EU Environmental Technology Action Plan (ETAP) when reporting to the Spring Council 2005. Member States should set a road map for the implementation of ETAP, identifying concrete measures and deadlines, in particular as regards its research dimension (notably technology platforms) and SME support (risk capital) and getting prices right through the removal of harmful subsidies.*

[11] See report from the World Resources Institute : “Changing Drivers: The impact of climate change on competitiveness and value creation in the automotive industry”. http://business.wri.org/pubs_description.cfm?PubID=3873

Thirdly even without fiscal measures, which can be helpful, governments can support eco-efficient innovation further. They can stimulate markets for eco-innovations through greening public procurement. By acting as a launching customer, governments can help eco-efficient innovations, as other potential purchasers are able to examine the performance of these new technologies. Furthermore green public procurement can help bring down costs by creating economies of scale.

***Key recommendation***

*National and local authorities should set up action plans for greening public procurement by the end of 2006* [12]*, focusing in particular on renewable energy technology and new vehicle fuels. The Commission should facilitate the dissemination of good practice among Member States and public authorities.*

***Working on a sustainable future***

The sustainability challenge calls for individual policies adopted in the short-term to be consistent with the EU's long-term objectives. In the context of the Lisbon-strategy, this requires consistency between the short-term and long-term objectives, thus balancing policies designed to boost growth and employment and environmental objectives. Concerns have been raised that environmental action aimed at meeting long term sustainable development objectives affects the competitiveness of some sectors unless competing nations take similar action. This could lead to delays of environmental action. The challenge in this context is to find the right balance between economic, social and environmental dimensions when designing and making policy choices. The EU and Member States need to pursue the development of impact assessment tools in order to help them make well informed decisions, where all costs and benefits, including short and long-term ones, are taken into consideration. This is unavoidable if Europe wants to continue with its leadership to the rest of the world in the area of environment without neglecting the impact it has on growth and employment.

Europe must pursue the long-term objective of increasing energy and resource efficiency. Recent increases and fluctuations in oil prices caused by geopolitical factors highlight the EU's increasing dependence on foreign oil imports (82% in 2002). Increasing energy efficiency and further developing alternative energy sources will not only help to reduce this dependence but could also serve the EU's competitiveness by bringing down the energy bill.

The actions above can be supported by the continued improvement of the environmental policy toolkit in order to promote better regulation. The new approach to environmental policy that the EU and Member States have adopted in recent years needs to be continued. Such an approach consists of setting long term targets without prescribing the technological means to achieve these targets.



[12] In Integrated Product Policy (IPP) Communication COM (2003) 302 final.

# Chapter Three - Making Lisbon work

The Lisbon strategy aims to raise Europe's growth and employment, and to embed the European commitment to social cohesion and the environment in the heart of the growth process – to be a means of growth rather than a claim on it. In our view the radical stepping up of Europe's efforts to construct its knowledge economy, the construction of a single market in goods and services and a climate that genuinely fosters business and enterprise will go a long way to achieving this goal, combined with the approach the High Level Group has advocated on the labour market and environment. But the delivery of such sustainable economic growth, however well supported with growth oriented monetary and fiscal policies, comes with tough options and choices; resources have to be refocused and vested interests challenged. Structural change is never easy. Nonetheless, security is not achieved by resisting or delaying reform. It is by embracing change that the social and environmental results European value can be preserved and even improved.

Unfortunately progress to date has been inadequate largely due to lack of commitment and political will. More political ownership is the precondition for success. At the same time there needs to be more coherence and consistency between Lisbon's means and ends together with a thorough overhaul and redesign of the processes for implementation and communication. When the European Union has succeeded in the recent past – such as the launch of the 1992 Single Market, the establishment of the single currency and European enlargement – it has been because the European institutions and Member States have worked closely together in what was understood to be a great and necessary project that had to be implemented as crucial to Europe's future. The Lisbon strategy for growth and employment is an equally important project. The European Commission and Member States together with social partners and other stakeholders throughout Europe must now show that they are committed to the Lisbon process and accept their responsibility in implementing the agreed reform programme. Governments and the European Commission must take the political lead that is so vitally required.



***Key recommendation***

*The 2005 Spring European Council should revitalise the Lisbon strategy. It should send a clear message to engage national governments and citizens in implementation. The European Council must consistently ensure that sufficient time and attention are consecrated to assessing the progress in achieving the Lisbon goals.*

*The High Level Group advises the EU and Member States to focus on growth and employment in order to underpin social cohesion and sustainable development.*

*The President of the Commission should focus his mandate on driving the Lisbon strategy forward.*

***Promoting coherence and consistency in implementation***

It is clear that the progress of the Lisbon strategy has suffered from incoherence and inconsistency, both between participants and between policies. Coherence and consistency means that those involved should all be aware of and share the same goal. Policies pulling in contradictory or opposite directions must be realigned so that instead they are mutually reinforcing. To achieve the goals of more growth and employment means ensuring that there is clear alignment between participants, policies and objectives.

Member States inevitably play a crucial role in achieving growth and employment – not only for their own countries but because in an European context a good performance by one Member State will lift the performance of other Member States and vice versa. As the High Level Group has said, a rising European tide lifts every European boat. The lack of commitment at both the national and European level has meant that these benefits have not been captured, exposing inconsistencies and incoherence. Europe as a whole can no longer pay the price in lost employment and foregone growth.

Up until now national parliaments and citizens have been too little associated with the process, so that pressure on governments has been less than it should and could have been. The same applies to social partners and other stakeholders. Closer co-operation between the various stakeholders is needed, who must commit themselves to the process of encouraging and supporting each other. All of this confirms the need for a partnership for reform constructed within each Member State's particular national context.

***Key recommendation***

*The 2005 Spring European Council should indicate what progress has been made in establishing partnerships for reform, called for in the 2004 Spring Council, in order to gather citizens, social partners, stakeholders and public authorities around the key priorities of growth and employment.*



Transparency about the progress achieved is the key to involving those stakeholders – as is the political will and commitment to advancing the agenda. An overview of the intended measures to be taken by governments is pivotal to achieving such transparency. Therefore the High Level Group calls upon each Member State under the leadership of the Head of the Government to formulate a national action programme, setting out road maps, including milestones, about how it is going to achieve the Lisbon targets. This approach serves three goals: it corrects the absence of national involvement in the Lisbon strategy, it helps ensure coherence and consistency between measures taken and it involves all stakeholders.

In order to ensure coherence and consistency of the national measures, Heads of State and Government must signal their commitment to their particular national strategy. A designated member of each government could be charged with carrying the day to day implementation of Lisbon forward. National parliaments must take more ownership of Lisbon, interpreting it to their national publics and by debating what to do or not to do, opening up the whole issue. In order to benefit from their expertise and to commit them to future implementation, involvement of social partners and other stakeholders – the partnership for growth and employment - is also needed in the formulation of the road maps. In order not to lose political momentum, these strategies should cover two years, and be renewed in 2007.

***Key recommendation***

*At the 2005 Spring Council Heads of State and Government should commit themselves to deliver the agreed reforms. National governments should present a national action programme before the end of 2005. In order to engage all the forces around this key* *objective, these national plans should be subject to debate with national parliaments and social partners.*

The effort to promote coherence and consistency then needs to be extended between Member States so that it continues and is reinforced at European level. The action programmes should be submitted to the European Commission. The European Commission should draw up a precise analysis of the 25 plans and specific recommendations on each one in its synthesis report for the Spring European Council of 2006. To further enhance coherence and consistency between the national and the European level, the national road maps should take into account the joint European principles of economic and employment policy, as laid down in the Broad Economic Policy Guidelines (BEPG's) and Employment Guidelines. However first the consistency and coherence of these two instruments must be further enhanced. Currently they are perceived as representing two separate worlds, while in fact both cover crucial elements of growth in Europe. They should be both adapted and better streamlined with the Lisbon process to support growth and employment objectives and guarantee cross-fertilisation.

***Key Recommendation***

*The Spring Council should invite the Council to adopt at the latest by July 2005 the BEPG's and Employment Guidelines, which must fully reflect the focused objectives of growth and employment. These guidelines should be adopted for a cycle of four years, covering two cycles of national programmes, in order to ensure both instruments are as coherent and internally consistent as possible.*



Coherence between the institutions of the European Union is required as well. Therefore the European Parliament needs to be involved much more in this process. It must hold the European Commission accountable for the progress it is making and the way it is discharging its responsibilities. This requires an active role of the Parliament itself, as the much-applied Open Method of Co-ordination in the Lisbon strategy does not provide it an automatic role. Therefore the European Parliament could consider setting up a standing committee on the Lisbon strategy for growth and employment.

***Key Recommendation***

*The European Parliament could establish a standing committee on the Lisbon strategy for growth and employment.*

The potential of the Parliament to hold key players to account should offer the European Commission a further incentive to deliver on its undertakings. Finally the European stakeholders, especially the social partners, must provide - through their active involvement - a link and thus a consistency between the national and the European level. They should enrich the debate on growth and employment, take up their part of the responsibility and adopt the implementation of Lisbon as part of their common work programme.

A better reflection of the priorities of the European Union in its budget would further enhance the coherence at the European level. The Union should not only persuade Member States to implement Lisbon; it should back up its words as far as possible with financial incentives. Under the current Community budget framework, major sums are already devoted — directly or indirectly — to growth, employment and competitiveness.

Whatever decisions are finally reached about the absolute level of Community spending in the next multi-annual budget, the so-called financial perspectives, the High Level Group believes that the structure of the European budget must reflect the priorities of the Lisbon strategy - as should national budgets. R&D, infrastructure spending and education and training are examples of spending that promotes economic competitiveness. The EU budget should be reshaped so EU spending reflects the priority accorded to growth and employment. In addition this reshaping should include an analysis of the possibilities to introduce budgetary incentives to encourage Member State achievement of Lisbon targets.

***Key recommendation***

*The EU Budget should as far as possible be reshaped to reflect the Lisbon priorities. Part of this reshaping should be an analysis of the possibilities to introduce budgetary incentives to encourage Member State achievement of Lisbon targets.*



***Improving the process for delivery***

The Open Method of Co-ordination has fallen far short of expectations; if Member States do not enter the spirit of mutual benchmarking, little or nothing happens. But neither has the Community method delivered what was expected. Member States are lagging behind the implementation of what has been agreed; the transposition of directives is in almost all Member States far behind the target. If governments do not show commitment to implementation nationally, this remains a huge problem. Furthermore, in too many cases, implementing legislation is not in line with the original Directive or is excessively complex, negating the benefits intended to stem from a single set of rules and often placing unnecessary burdens on business. It is clear that both methods depend to a high degree on political will.

The central elements of the Open Method of Co-ordination - peer pressure and benchmarking - are clear incentives for the Member States to deliver on their commitments by measuring and comparing their respective performance and facilitating exchange of best practice. The High Level Group proposes a radical improvement of the process, making better use of the fourteen indicators and then better communicating the results in order to ratchet up the political consequences of non-delivery.

More than a hundred indicators have been associated to the Lisbon process, which makes it likely that every country will be ranked as best at some indicators. This makes this instrument too ineffective. Member States are not challenged to improve their record. Simplification is vital. The establishment by the European Council of a more limited framework of fourteen targets and indicators offers the opportunity to improve the working of this instrument of peer pressure. The High Level Group considers this list to represent the best trade-off between keeping Lisbon simple and capturing its ambition and comprehensiveness. The European Commission should present to the Heads of State and Government and the wider public annual updates on these key fourteen Lisbon indicators in the format of league tables with rankings (1 to 25), praising good performance and castigating bad performance – naming, shaming and faming. These fourteen indicators offer the opportunity for Member States further to emphasise the growth and employment dimension of Lisbon if they choose.

Not all Member States start with the same position, especially those who have recently joined. For them the message needs to be more nuanced and calibrated, recognising the economic reality that they started from a very low base. Even if the statistical target remains still distant, if they have made significant progress they should nonetheless be praised.

***Key recommendation***

*The European Commission should deliver an annual league table of Member State progress towards achieving the fourteen key indicators and targets to the Spring European Council in the most public manner possible. Countries that have performed well should be praised; those that have done badly castigated.*

***Communication***

The challenges facing Europe, why policies are developing as they are and the importance of acting together need to be understood much better by the European public. Understanding requires clear and vigorous communication whose importance for the success of the Lisbon project can not be underestimated. All involved, including European and national politicians, have an important role to play in delivering the message.

The public process of benchmarking offers the opportunity to communicate to a wider audience about the strategy for growth and employment and the progress made. The proposals the High Level Group has made – national action programmes, the greater involvement of Member States and parliaments, the ongoing and heightened role of the Spring European Summits in progressing Lisbon – will provide a great many opportunities for debate, argument and discussion. They must be seized. The same pro-activity, using the best modern communication methods, should extend to communications of the European Commission. The High Level Group recommends a review of the European Commission’s communications and communication strategy to ensure that they meet the highest possible standards.

***Key Recommendation***

*Communications and communication strategy within the European Commission should be reviewed and where necessary reformed to ensure they meet the highest possible standards before the Spring European Council in 2005.*

***Conclusion***

Europe’s leaders need to instil hope that tomorrow will be better than today. Europe has considerable economic and social strengths, as the High Level Group has identified. The programme of reform outlined in this report is eminently deliverable and will bring improvement. It needs to be clearly understood and explained, and then delivered; the act of delivery, along with the associated improvement, will start to put Europe on a virtuous circle of better economic performance, rising confidence and expectations, and improved trust.

Changes such as the opening up of markets, the modernisation of social policy, pensions and health-care systems, promoting the adaptability of the labour market or even education systems have an immediate impact on peoples' daily lives. Many of these changes are positive, unlike the common portrayal; for example more competition empowers consumers, improved care for children and the elderly enhances the lives of carers, typically women, while access to life-long education offers workers the chance of mobility, self-improvement and greater opportunity. However unless the programme is understood as a comprehensive package, each component will not be given the chance to prove it can work and contribute to generalised improvement. The chance of moving on to a virtuous circle of improved performance and trust will be greatly reduced.

The need for reform has to be explained especially to citizens who are not always aware of the urgency and scale of the situation. "Competitiveness" is not just some dry economic indicator often unintelligible to the men in the street, but provides a diagnosis of the state of economic health of a country or a region. In the present circumstances, the clear message must be: if we want to preserve and improve our social model we have to adapt: it is not too late to change. In any event the status quo is not an option. Engaging and involving citizens in the process serves two mutually reinforcing attractions: it in effect seeks public support by giving people elements for debate and it leverages that support to put pressure on government to pursue these goals.

The High Level Group is not calling for indiscriminate action; reform packages should be balanced, well thought through and properly designed. Equally, we call for a strengthening and modernisation of the distinctive European approach to organising economy and society, so embedding core European values that all Europeans care about. The issue is delivering on the promises and undertakings that have been made, and that will entail significant change.

The promotion of growth and employment in Europe is the next great European project. Its execution will require political leadership and commitment of the highest order, along with that of the social partners whose role the High Level Group wishes to sustain. However the privilege of voice and participation is accompanied by responsibility which we urge all to accept. The citizens of Europe deserve no less.

The measures we propose require - in our European democratic system – sustained political determination. In the end, much of the Lisbon strategy depends on the progress made in the national capitals: no European procedure or method can change this simple truth. Governments and especially their leaders must not duck their crucial responsibilities. Nothing less than the future prosperity of the European model is at stake.

# ANNEXES

**Relative performance of the Old Member States according to the structural indicators on the shortlist [1]**

| Levels [2] | | AT | BE | DE | DK | ES | FI | FR | GR | IE | IT | LU | NL | PT | SE | UK | | EU25 | EU15 | | US | | Target 2005 | Target 2010 |
|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|
| GDP per capita (PPS, EU 15 = 100) | 2003 | 111,4 | 106,6 | 98,8 | 112,9 | 87,3 | 100,6 | 103,8 | 73,0 | 121,7 | 97,8 | 194,6 | 109,9 | 68,3 | 105,6 | 108,9 | | 91,2 | 100,0 | | 140,3 | | | |
| Labour productivity per person employed (PPS, EU 15 = 100) | 2003 | 96,4 | 118,4 | 94,3 | 97,8 | 94,8 | 98,6 | 113,7 | 90,3 | 119,7 | 103,6 | 132,2 | 95,2 | 63,5 | 96,5 | 101,9 | | 93,1 | 100,0 | | 121,6 | | | |
| Employment rate (%) [3] | 2003 | 69,2 | 59,6 | 65,0 | 75,1 | 59,7 | 67,7 | 63,2 | 57,8 | 65,4 | 56,1 | 62,7 | 73,5 | 67,2 | 72,9 | 71,8 | | 62,9 | 64,4 | | 71,2 | | 67,0 | 70,0 |
| Employment rate females (%) [3] | 2003 | 62,8 | 51,8 | 59,0 | 70,5 | 46,0 | 65,7 | 57,2 | 43,8 | 55,8 | 42,7 | 52,0 | 65,8 | 60,6 | 71,5 | 65,3 | | 55,1 | 56,0 | | 65,7 | | 57,0 | 60,0 |
| Employment rate of older workers (%) | 2003 | 30,4 | 28,1 | 39,5 | 60,2 | 40,8 | 49,6 | 36,8 | 42,1 | 49,0 | 30,3 | 30,0 | 44,8 | 51,1 | 68,6 | 55,5 | | 40,2 | 41,7 | | 59,9 | | | 50,0 |
| Educational attainment (20-24) (%) | 2003 | 83,8 | 81,3 | 72,5 | 74,4 | 63,4 | 85,2 | 80,9 | 81,7 | 85,7 | 69,9 | 69,8 | 73,3 | 47,7 | 85,6 | 78,2 | | 76,7 | 73,8 | | | | | |
| Research and development expenditure (% of GDP) | 2003 | 2,2 | 2,2 | 2,5 | 2,5 | 1,0 | 3,4 | 2,2 | 0,6 | 1,2 | 1,1 | 1,7 | 1,9 | 0,9 | 4,3 | 1,9 | | 1,9 | 2,0 | | 2,8 | | | 3,0 |
| Business investment (% GDP) | 2003 | 20,3 | 17,9 | 16,3 | 18,2 | 22,1 | 15,3 | 15,9 | 21,8 | 19,7 | 16,5 | 15,0 | 16,5 | 19,1 | 12,6 | 14,6 | | 16,8 | 16,7 | | | | | |
| Comparative price levels (EU 15 =100) | 2002 | 102 | 99 | 104 | 131 | 82 | 123 | 100 | 80 | 118 | 95 | 100 | 102 | 74 | 117 | 108 | | 96 | 100 | | 113 | | | |
| At-risk-of-poverty rate (%) | 2003 | 12,0 | 13,0 | 11,0 | 10,0 | 19,0 | 11,0 | 15,0 | 20,0 | 21,0 | 19,0 | 12,0 | 11,0 | 20,0 | 9,0 | 17,0 | | 15,0 | 15,0 | | | | | |
| Long-term unemployment rate (%) | 2003 | 1,1 | 3,7 | 4,6 | 1,1 | 3,9 | 2,3 | 3,5 | 5,1 | 1,5 | 4,9 | 0,9 | 1,0 | 2,2 | 1,0 | 1,1 | | 4,0 | 3,3 | | | | | |
| Dispersion of regional employment rates | 2003 | 3,1 | 7,7 | 6,0 | - | 8,9 | 6,1 | 5,0 | 3,6 | - | 17,0 | - | 2,4 | 3,9 | 4,3 | 6,0 | | 13,0 | 12,0 | | | | | |
| Greenhouse gases emissions (Index base year=100) | 2002 | 108,5 | 102,1 | 81,1 | 99,2 | 139,4 | 106,8 | 98,1 | 126,5 | 128,9 | 109 | 84,9 | 100,6 | 141 | 96,3 | 85,1 | | 91,0 | 97,1 | | 113,1 | | | 92,0 |
| Energy intensity of the economy | 2002 | 146 | 214 | 165 | 123 | 229 | 272 | 187 | 258 | 164 | 184 | 198 | 202 | 254 | 224 | 212 | | 210 | 191 | | 330 | | | |
| Volume of transport | 2002 | 120 | 100 | 102 | 85 | 137 | 95 | 96 | 127 | 133 | 103 | 110 | 97 | 126 | 90 | 86 | | 101 | 102 | | 91 | | | |

1. Source: Eurostat, if not stated otherwise. For a detailed definiton of and explanatory notes on the indicators as well as on single values go to: http://europa.eu.int/comm/eurostat/structuralindicators. 2. Levels for the year indicated or for the last available year. 3. Employment data US: source OECD.

**Relative improvement in the performance of the Old Member States according to the structural indicators on the shortlist [1]**

| Evolution [2] | | AT | BE | DE | DK | ES | FI | FR | GR | IE | IT | LU | NL | PT | SE | UK | EU25 | EU15 | US |
|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|
| GDP per capita | 1999-2003 | 1,2 | 1,2 | 0,8 | 1,1 | 2,1 | 2,3 | 1,4 | 3,9 | 4,8 | 1,1 | 2,9 | 0,5 | 0,4 | 1,9 | 2,1 | 1,5 | 1,4 | 1,2 |
| Labour productivity per person employed | 1999-2003 | 1,1 | 0,8 | 0,7 | 1,7 | 0,6 | 1,4 | 0,6 | 3,9 | 3,6 | -0,4 | -0,1 | 0,1 | 0,2 | 1,2 | 1,7 | 1,0 | 0,7 | 1,9 |
| Employment rate [3] | 1999-2003 | 0,2 | 0,1 | -0,1 | -0,2 | 1,5 | 0,3 | 0,6 | 0,6 | 0,5 | 0,9 | 0,3 | 0,4 | -0,1 | 0,3 | 0,2 | 0,3 | 0,5 | -0,7 |
| Employment rate females [3] | 1999-2003 | 0,8 | 0,4 | 0,4 | -0,1 | 1,9 | 0,6 | 0,8 | 0,8 | 0,9 | 1,1 | 0,9 | 0,9 | 0,3 | 0,5 | 0,3 | 0,6 | 0,8 | -0,5 |
| Employment rate of older workers | 1999-2003 | 0,2 | 0,9 | 0,4 | 1,4 | 1,5 | 2,7 | 2,0 | 0,8 | 1,3 | 0,7 | 0,9 | 2,1 | 0,2 | 1,2 | 1,5 | 1,0 | 1,2 | 0,5 |
| Educational attainment (20-24) | 1999-2003 | -0,2 | 1,3 | -0,5 | 0,3 | -0,4 | -0,4 | 0,2 | 0,6 | 0,9 | 0,9 | -0,4 | 0,3 | 1,9 | -0,2 | 0,7 | 0,5 | 0,3 | |
| Research and development expenditure | 1999-2003 | 0,07 | 0,11 | 0,02 | 0,14 | 0,05 | 0,05 | 0,00 | -0,02 | -0,02 | 0,04 | | -0,07 | 0,05 | 0,31 | 0,01 | 0,03 | 0,02 | 0,03 |
| Business investment | 1999-2003 | -0,02 | -0,28 | -0,83 | 0,02 | 0,33 | -0,38 | -0,07 | 0,65 | -0,33 | -0,03 | -1,10 | -0,75 | -1,00 | -0,38 | -0,30 | -0,25 | -0,30 | |
| Comparative price levels | 1999-2002 | 0,4 | -1,8 | 0,0 | 2,5 | 0,4 | 1,2 | -1,7 | -1,2 | 4,9 | 1,3 | 0,5 | 0,4 | 0,8 | -1,0 | 0,1 | 0,2 | 0,0 | 4,4 |
| At-risk-of-poverty rate | 1999-2003 | 0,0 | 0,0 | 0,0 | -0,5 | 0,0 | 0,0 | 0,0 | -0,5 | 1,0 | 0,5 | -0,5 | 0,0 | -0,5 | 0,0 | -1,0 | 0,0 | 0,0 | |
| Long-term unemployment rate | 1999-2003 | 0,0 | -0,3 | 0,1 | 0,0 | -0,5 | -0,2 | -0,2 | -0,3 | -0,2 | -0,5 | 0,1 | -0,1 | 0,1 | -0,2 | -0,2 | 0,0 | -0,2 | |
| Dispersion of regional employment rates | 1999-2003 | 0,2 | -0,1 | 0,2 | - | -0,5 | -0,2 | -0,5 | -0,4 | - | -0,1 | - | 0,0 | 0,3 | -0,2 | -0,3 | -0,1 | -0,5 | |
| Greenhouse gases emissions | 1999-2002 | 1,9 | 0,4 | -0,1 | -2,0 | 3,4 | 2,0 | -0,6 | 3,6 | 1,6 | 0,9 | 4,6 | 0,2 | 1,2 | -0,2 | -0,6 | 0,1 | 0,3 | 0,4 |
| Energy intensity of the economy | 1999-2002 | 0,7 | -10,0 | -1,3 | -3,0 | 0,7 | -1,3 | -1,7 | -1,7 | -5,7 | -3,3 | 1,7 | 0,0 | 2,3 | -4,7 | -7,3 | -2,7 | -2,3 | -4,0 |
| Volume of transport | 1999-2002 | 3,0 | 7,0 | -0,6 | -2,8 | 8,6 | -0,9 | -2,8 | -5,0 | 3,9 | 0,6 | 7,1 | -2,7 | 3,2 | -0,3 | -2,5 | -0,1 | 0,0 | -0,8 |

1. Source: Eurostat, if not stated otherwise. For a detailed definiton of and explanatory notes on the indicators as well as on single values go to: http://europa.eu.int/comm/eurostat/structuralindicators. 2. Evolution for the period indicated or for the closest available period. Average annual real growth rate % for GDP per capita and Labour productivity, Average annual percentage point change for the other indicators. 3. Employment data US: source OECD.

**Relative performance of the New Member States according to the structural indicators on the shortlist [1]**

| Levels [2] | | CY | CZ | EE | HU | LT | LV | MT | PL | SI | SK | EU25 | EU15 | US | Target 2005 | Target 2010 |
|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|
| GDP per capita (PPS, EU 25 = 100) | 2003 | 76,3 | 66,5 | 42,5 | 55,6 | 41,9 | 38,8 | 68,1 | 42,2 | 70,6 | 46,8 | 91,2 | 100,0 | 140,3 | | |
| Labour productivity per person employed (PPS, EU 15 = 100) | 2003 | 77,1 | 61,3 | 43,1 | 62,8 | 44,4 | 40,1 | 82,3 | 49,6 | 70,0 | 54,1 | 93,1 | 100,0 | 121,6 | | |
| Employment rate (%) [3] | 2003 | 69,2 | 64,7 | 62,9 | 57,0 | 61,1 | 61,8 | 54,2 | 51,2 | 62,6 | 57,7 | 62,9 | 64,4 | 71,2 | 67,0 | 70,0 |
| Employment rate females (%) [3] | 2003 | 60,4 | 56,3 | 59,0 | 50,9 | 58,4 | 57,9 | 33,6 | 46,0 | 57,6 | 52,2 | 55,1 | 56,0 | 65,7 | 57,0 | 60,0 |
| Employment rate of older workers (%) | 2003 | 50,4 | 42,3 | 52,3 | 28,9 | 44,7 | 44,1 | 32,5 | 26,9 | 23,5 | 24,6 | 40,2 | 41,7 | 59,9 | | 50,0 |
| Educational attainment (20-24) (%) | 2003 | 82,2 | 92,0 | 81,4 | 85,0 | 82,1 | 74,0 | 43,0 | 88,8 | 90,7 | 94,1 | 76,7 | 73,8 | | | |
| Research and development expenditure (% of GDP) | 2003 | 0,3 | 1,2 | 0,8 | 1,0 | 0,7 | 0,4 | | 0,6 | 1,5 | 0,6 | 1,9 | 2,0 | 2,8 | | 3,0 |
| Business investment (% GDP) | 2003 | 14,1 | 22,4 | 25,0 | 19,8 | 17,8 | 22,9 | | 14,9 | 21,1 | 23,2 | 16,8 | 16,7 | | | |
| Comparative price levels (EU 15 =100) | 2002 | 83 | 53 | 61 | 55 | 51 | 54 | 72 | 58 | 73 | 44 | 96 | 100 | 113 | | |
| At-risk-of-poverty rate (%) | 2003 | 16,0 | 8,0 | 18,0 | 10,0 | 17,0 | 16,0 | 15,0 | 15,0 | 11,0 | 21,0 | 15,0 | 15,0 | | | |
| Long-term unemployment rate (%) | 2003 | 1,1 | 3,8 | 4,6 | 2,4 | 6,1 | 4,3 | 3,5 | 10,7 | 3,4 | 11,1 | 4,0 | 3,3 | | | |
| Dispersion of regional employment rates | 2003 | - | 5,8 | - | 8,5 | - | - | - | 7,2 | - | 7,6 | 13,0 | 12,0 | | | |
| Greenhouse gases emissions (Index base year=100) | 2002 | 150 | 74,3 | 44,8 | 69 | 39,8 | 36,9 | 128,5 | 67,7 | 98,7 | 71,8 | 91,0 | 97,1 | 113,1 | | 92,0 |
| Energy intensity of the economy | 2002 | 280 | 921 | 1156 | 564 | 1273 | 759 | 264 | 650 | 343 | 964 | 210 | 191 | 330 | | |
| Volume of transport | 2002 | 93 | 100 | 177 | 91 | 119 | 123 | | 70 | 92 | 62 | 101 | 102 | 91 | | |

1. Source: Eurostat, if not stated otherwise. For a detailed definiton of and explanatory notes on the indicators as well as on single values go to: http://europa.eu.int/comm/eurostat/structuralindicators. 2. Levels for the year indicated or for the last available year. 3. Employment data US: source OECD.

| **Table A15** | Old-age dependency ratio | | | | | | | | | | |
|---|---|---|---|---|---|---|---|---|---|---|---|
| | **2000** | **2005** | **2010** | **2015** | **2020** | **2025** | **2030** | **2035** | **2040** | **2045** | **2050** |
| | | | | | | | | | | | |
| **B** | 26 | 26 | 27 | 30 | 33 | 37 | 42 | 45 | 46 | 46 | 45 |
| **DK** | 22 | 23 | 27 | 29 | 32 | 34 | 38 | 39 | 40 | 38 | 36 |
| **D** | 24 | 28 | 30 | 31 | 34 | 38 | 44 | 50 | 50 | 49 | 49 |
| **EL** | 26 | 28 | 29 | 31 | 33 | 35 | 38 | 43 | 47 | 52 | 54 |
| **E** | 25 | 26 | 27 | 29 | 31 | 34 | 39 | 45 | 52 | 58 | 60 |
| **F** | 24 | 25 | 25 | 29 | 33 | 36 | 40 | 43 | 45 | 45 | 46 |
| **IRL** | 17 | 17 | 17 | 20 | 22 | 25 | 27 | 29 | 33 | 37 | 40 |
| **I** | 27 | 29 | 31 | 34 | 37 | 40 | 46 | 53 | 59 | 62 | 61 |
| **L** | 21 | 23 | 24 | 26 | 28 | 32 | 36 | 40 | 41 | 40 | 38 |
| **NL** | 20 | 21 | 22 | 26 | 30 | 33 | 38 | 42 | 44 | 42 | 41 |
| **A** | 23 | 25 | 27 | 30 | 32 | 37 | 45 | 52 | 54 | 54 | 54 |
| **P** | 23 | 25 | 25 | 27 | 29 | 31 | 33 | 37 | 41 | 45 | 46 |
| **FIN** | 22 | 23 | 25 | 31 | 36 | 39 | 43 | 44 | 43 | 43 | 44 |
| **S** | 27 | 27 | 29 | 33 | 35 | 37 | 40 | 41 | 42 | 42 | 42 |
| **UK** | 24 | 24 | 24 | 27 | 29 | 32 | 37 | 41 | 43 | 42 | 42 |
| **EU** | 24 | 26 | 27 | 30 | 32 | 36 | 41 | 45 | 48 | 49 | 49 |

Population aged 65+ as % of population aged 15 to 64

Source: Commission calculation based on Eurostat – central scenario