

Speech for Commissioner Hübner
San Marino Economic Forum,
San Marino
7 June 2008
'EU Policies supporting structural change'

Ladies and Gentlemen,

I would like to share with you my views on Europe's capacity to turn challenges into opportunities.

You can tell many different stories about the EU – one of the most fascinating would certainly be history of enlargements. One interesting aspect of the enlargement story would be the explanation of the power of attraction of the Union that started 51 years ago with six member states and reached 50 years later the membership of 27 with 6 queuing to join.

The EU has become one of the world's key economic engines, accounting for about 30% of global GDP and 20% of global trade flows, and 7% of global population while the euro has emerged as a key international currency. This is of course remarkable, and already the result of decades of reforms and adjustment. We can be proud of these results, often unthinkable, happening in Europe but we must not be complacent, as we are all facing with other parts of the world dramatic challenges. They are well known by now. I am thinking here about the structural shift in the global balance towards the emerging economies, the diverse demographic dynamics, the asymmetric effect of climate change, the structural inefficiencies in the energy markets, increased integration of global markets, spreading out effects of whatever we do or refrain from doing across the world, and - on the more topical side - I

would add the distortions in the global food markets and the turmoil in the financial markets.

While some of these problems can be corrected more easily, the major challenges will not go away, on the contrary they will accompany us for the time to come and they will trigger waves of deep structural changes. Europe's success, growth and well-being will depend on its capacity to respond to these challenges.

What seems also clear is that instead of fearing the necessary changes, we should better embrace them. Of course structural change means both creation and destruction. We must nurture and develop the creative forces while mitigating the impact of the destructive ones. That is why we should orchestrate the process of structural change and that is why I believe that wise genuine public-private partnership is a way to go.

Public policies should give the private sector a helping hand in undergoing change. The public sector cannot do the job for the private actors, it can, however, create favourable conditions. What we need is private initiative, creativity and massive private investment, which can also come in the form of public-private partnership, but there is a long way to go.

Big restructuring is not something we would not know from the past. Actually, in the European Union we have 50 years of experience of bringing about and supporting structural change. The European Community was born in a time of great post-war structural change with European industry rapidly restructuring in the coal, steel and ship building sectors and a unanimously perceived need to regulate and

control this restructuring as well as the agriculture market. Over time the urge to regulate and control has faded. In agriculture a regime which covered almost every commodity and which did ensure a supply of food, in fact tones of excessive supply and a measure of security for farmers is rapidly being relaxed. We see we need more market here and any policy isolating farmers from the market incentives can only lead to global shortages. So in general I would say that the tendency now is for the European community to create conditions in which Europe's economy can flourish rather than to establish regimes which try to control it.

Typical of policy aimed at creating conditions is the Single European Internal Market which was developed between 1985 and 1992 and swept away many of the barriers to economic activity. The single market is at the heart of today's Union, it is home to 500 million citizens and over 20 million businesses, with people, goods, services and money that may move around as if within one country. With trade barriers removed and national markets opened, within the framework of rather tough European competition policy, more firms can compete against each other. Trade enhances growth. It brings consumers a wider range of products to chose from. Competition between imports and local products has generally lowered prices and raised quality as it was expected to do.

The disappearance of trade barriers within the EU has made a significant contribution to its prosperity, by boosting growth and employment. Since its beginning in 1992, the Single Market has created nearly three million extra jobs and recent enlargements have given it a new impetus. The estimated macroeconomic gains from the internal market are sizeable, amounting to approximately 1,8% EU GDP and 1,4% of total employment.

However, implementing modern Single Market policy is a complex task and we have not yet finished the job. We are still working in certain areas like energy and financial services to truly open the market up. And we want to live in a knowledge economy, where human capital creativity innovation and productivity matter most. The Single Market is capable of strengthening the development of knowledge and innovation in the EU. But if it is to do so, we need to do more to promote the free movement of knowledge and innovation as a "fifth freedom" in the internal market. And that is what we are working on at the EU, national, regional and local levels.

Another example of a policy creating conditions for growth and structural change is European Monetary Union. By joining the EMU, 15 countries have replaced their national currencies with the Euro and given up their independent monetary policy to the European Central Bank. The Euro has fast become the world's second most important currency. In parallel, the institutions of EMU have earned a high degree of respect and recognition. The EMU has anchored macroeconomic stability in Europe by putting an end to periods of internal currency turbulence within the Euro area and making it more resilient to negative external developments. The result has been a decade of low and stable inflation. Just a few days ago (29 May) the governor of the European Central Bank, Jean Claude Trichet emphasised how effective the currency has been in standing up to a series of economic shocks recently which would have caused chaos in the old system of national currencies. In the past in periods like the one we are going through everybody was reaching out to Deutsch Mark and all weak currencies suffered.

The Euro has delivered new opportunities for the development of financial markets and has spurred their integration, fostering deeper and more liquid bond and money markets in Europe. The movement of cross-border capital towards its best use has been encouraged, as well as risk diversification and associated cyclical smoothing. Where we seem to be condemned to go now is towards more of financial market surveillance.

While the policies I just discussed delivered impressive results, it did not generate an efficient framework or mechanism that ensures that structural change is a constant process. To use Darwin's wisdom I would say that as for any successful species, our capacity to adjust determines our success or failure.

So, we have come up with the growth and jobs and competitiveness or 'Lisbon' strategy, in order to put this idea into practice. The Lisbon strategy not only sets ambitious targets but is underpinned by a comprehensive set of reform instruments, ranging from the simplification of EU regulation, facilitating setting-up new business to our flexicurity approach. Originally it was intended to boost the European knowledge economy so that we could overtake the United States and grow faster than China, it is today much more realistic and has a number of functions.

One of these is to even out stresses in the Euro Zone which cannot be dealt with by the growth and stability pact alone. They arise from the absence of a fiscal transfer mechanism across its members and the relative weakness of alternative adjustment mechanisms like labour mobility or responsiveness of prices and wages to the business cycle. The Lisbon Strategy therefore has a growing role in orchestrating structural reforms in product, labour and financial markets. And let me say that it works.

The relatively strong economic performance since the renewal of the Lisbon Strategy in 2005 is of course partly related to the favourable economic cycle and a strong global demand. But the EU as a whole also strongly benefited from the fast growing economies of the new Member States after their accession to the EU.

The debate on whether the good recent economic results are a predominantly cyclical or a predominantly structural phenomenon may in the end remain academic. The important message for me is that the renewed Lisbon strategy has undoubtedly played a positive role for the implementation of structural reforms all around the EU; reforms which give us a good chance to boost Europe's competitiveness for the future. Our conclusion in December last year was therefore justified – the renewed strategy, based on an open and operational partnership, works. However it is plain that none of these policies by themselves, successful as they are, can have the influence to bring about all the structural changes needed in Europe's economy where businesses would continually shift their activities from less productive and less competitive sectors to sectors where they have a comparative advantage and which are likely to grow.

The challenge of structural change is raising productivity in a sustained way and this is best brought about by competition, which in turn boosts innovation based on knowledge and capacity to convert it into material reality.

Structural change implies big shifts of employment between industries and from industries to services. This means that a lot of people have to be retrained and many new businesses created, especially in the growth sectors.

And that is a good point to introduce the policy for which I am responsible, Cohesion Policy. It is a policy operating through a multilevel governance. This is an investment policy mobilizing the growth potential at the regional and local level, designed to enhance the attractiveness of Europe's regions to live, work and invest by improving transport, environmental and other infrastructure, encouraging regions to develop and outsiders to invest. It makes structural change possible through investing in new skills and promoting the culture of protecting workers instead of jobs. It encourages an atmosphere conducive to small and medium enterprise development, nurturing clusters, networking and facilitating technology transfer, and research and innovation facilities. It promotes cross border and trans-national co-operation in a wide range of activities which include regions in current and potential candidate countries like Croatia, Turkey and Serbia sharing best practice. It now incorporates mechanisms offering to entrepreneurs new forms of financial engineering. Its implementation is based upon a programming system and responsibilities which are devolved to local authorities which include a wide range of partners from central government, regional government, business and civil society. This makes the system uniquely effective.

The effect of this system with its budget of €350 billion is to catalyse change in the economic structures of Europe's regions. The money represents just 0.37% of Community GDP but what matters is its catalytic effect. It comes about from the fact that everything financed from the Community budget is matched or exceeded by local contributions both public and private. I estimate that the €350 billion I mentioned earlier will unlock at least another €700 billion from national

sources. For example Italy is scheduled to receive €28.8 billion but will add another €96 billion of its own resources to the programme. Add this to the fact that many Member States specifically align their own regional policies to the Community's priorities and the capacity for influence is clear.

So that is why we have harnessed this policy to deliver Lisbon Strategy. We have asked Member States to earmark a high proportion of their allocations to 'Lisbon' activities, essentially improving the attractiveness of regions, building up the knowledge economy, research and innovation.

This represents a step change in the direction of Cohesion Policy. The way we allocate resources has also changed in the sense that all regions are now eligible. Regions come into the **Convergence** Objective if below 75% of average GDP and for the **Competitiveness** Objective otherwise, with **transitional** status for those which were previously below 75% but have grown out of that category. Community money is invested therefore not on geographic criteria as in the past but on the basis of the potential for growth.

As a result, one of the biggest priorities put forward by Member States for the new period is research, technological development and innovation. In financial terms it will represent €86 billion or ¼ of investment in the next few years. This will enable us to make a substantial contribution to the original Lisbon target of spending 3% of total GDP on research.

The plans of the Member States also provide for action in favour of the environment which amounts to nearly one third of the total budget. One aspect of this is preventing and combating climate change (€48 billion), which covers investment in energy efficiency and renewable energies.

With this focus the public sector can facilitate what the private sector's job is - invest in an energy efficient economy and industry.

I did not talk about EU trade policy which has been fundamental to structural change and probably forgot or ignored many other relevant factors and instruments. But we are, I believe, in a period of dramatic change around the corner and already in our yard. We will soon wake up in a quite different world and Europe. I believe that it is better to be active and to fix the problems ourselves. The role of synergies between policies has grown. We need not only competition, but also a lot of cooperation. Processes of big structural change require some orchestration.