CENTRE FOR EUROPEAN REFORM

working paper

The Barcelona Scorecard

The status of economic reform in the enlarging EU

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Foreword

KPMG is delighted to sponsor the CER's second annual economic reform 'scorecard'. Two years on from the Lisbon summit – a watershed in European thinking on business issues – it is vital that the EU takes stock of what it has achieved and, equally importantly, what remains to be done. The CER's independent and hard-hitting perspective is a welcome contribution to that debate.

Since the last edition, the most fundamental change in the EU has been the arrival of euro notes and coins. These are now in daily use by 300 million Europeans. The successful launch shows what Europe can achieve when its member-states and EU institutions work together in pursuit of a common goal. The challenge of economic reform requires the same sense of purpose and co-ordinated effort. The EU's target of becoming the "world's most competitive and dynamic knowledge-based economy" by 2010 deserves nothing less.

I am particularly pleased to see that this edition also includes the EU candidate countries of Central and Eastern Europe. Their active participation in the Lisbon process is essential if the political 'iron curtain' that divided Europe for so long is not to be replaced by an economic divide. With our many offices from Belfast to Bucharest, KPMG knows very well how much these countries can contribute to a united Europe.

The global economy has come through a difficult year, but the Lisbon strategy provides a clear road-map of the way ahead for Europe. Businesses across the continent are ready to play their part. But political leaders must confront the hard choices and provide the necessary leadership that Europe badly needs, if we are to meet the challenge of competitiveness in the twenty-first century.

Mike Rake
European Chairman of KPMG

1 Introduction

Many Europeans like to think of their continent as a global economic superpower. But compared to the US over the last decade or so, Europe looks like a laggard. From 1990 to 2000, the EU achieved only one year of economic growth above 3 per cent. In contrast, the US economy experienced just one year in which its economy grew by *less* than 3 per cent. This year, having recovered from a short recession, the US looks set to grow much faster than Europe. Futhermore, emerging economies are poised to overtake the 'old continent' in an increasingly global marketplace: China's fast-growing GDP could approach the EU's within a decade or two.

To address these concerns, EU leaders, meeting in March 2000 in the Portuguese capital, agreed an ambitious ten-year programme of economic reform. The goal of the 'Lisbon agenda' was to make Europe "the most competitive and dynamic knowledge-based economy in the world" by 2010. This would require raising Europe's output by around 40 per cent and creating 20 million new jobs. The presidents and prime ministers agreed to meet each spring in order to maintain the momentum behind this process.

In March 2001, shortly before the second of these special European Council meetings, the CER published its own 'Lisbon Scorecard'. This working paper graded the EU's performance in meeting the targets set one year previously. The overall score was satisfactory but certainly not stellar. Despite the Swedish presidency's best efforts, many observers agreed that the Stockholm Council had failed to make much progress on some key issues, notably energy liberalisation.

Under the system of the EU's rotating presidency, responsibility for pushing forward the Lisbon agenda passed from Sweden via Belgium, to Spain, another strong advocate of structural economic reform. In the summer of 2001, British Prime Minister Tony Blair predicted that the Barcelona summit in mid-March 2002 would be "make or break" for the EU's economic reform agenda. This CER working paper follows up on the first edition of the 'Lisbon Scorecard'. It assesses whether the EU is on track for meeting the 2010 goal, and in particular whether the Barcelona meeting has brought any progress.

The Lisbon agenda employs a mixture of old and new approaches to policy-making. The traditional 'Community method' remains important when uniform legislation is needed: Commission proposals are debated and passed by the European Parliament and the Council of Ministers. But this approach has been supplemented by the new 'open method of co-ordination'. Overall objectives are still agreed at an EU level by the member-states. But national governments have more flexibility on how to achieve these objectives. Although the European Commission has no legislative role in this model, it has broadly embraced the Lisbon agenda. The Commission has developed a number of 'structural indicators', which benchmark EU member-states against each other and against other leading economies, in order to aid the exchange of best practice.

As with the previous edition, the CER's assessment of progress includes an important subjective element that focuses on the politics behind economic reform. Countries that are pushing hard for reform, as well as those that already show best practice, achieve 'hero' status in our scorecard. In contrast, those lagging badly, or showing little willingness to improve, are designated as 'villains'.

Over the last year, neither the economic nor the political contexts encouraged bold measures. The effect of the global downturn on EU economies had been more dramatic and direct than many had expected. The CER was not alone in forecasting, early last year, that the EU would be well placed to weather the recession which was then brewing in the US. But European businesses still depend heavily on the American economic cycle. Germany, the EU's largest economy and biggest exporter, has been particularly badly hit.

Of course, structural reform would help the EU to become less vulnerable to such external economic shocks. But in the short-term, reform often involves a heavy political cost in the form of job losses. And although a new round of global trade talks in the World Trade Organisation was successfully launched in Doha in November 2001, it will take many years before these negotiations translate into increased trade and economic growth. Therefore, Europe needs to take responsibility for its own malaise. The Lisbon agenda provides precisely the right prescription to remedy the EU's sickly economic performance.

Elections in two of Europe's largest economies have also slowed the pace of reform. France goes to the polls in May and June, Germany in September. Politicians in both countries have muffled talk of economic reform and the hard choices that come with it. The lack of a constructive French and German input into the Lisbon process has been the major drag on progress over the past year.

Over the medium and longer term, the impact of EU enlargement on Europe's economic performance will be profound. The member-states and the Commission have, belatedly, recognised this. They have therefore pledged to include the candidate countries in the Lisbon process from 2003, even before they become full members of the Union. This should not become an additional hurdle in the way of membership. After all, the Lisbon agenda neither replaces nor adds to the '*acquis communautaire*', the body of EU laws and rules that all candidates must adopt. But it is in everybody's interest that candidate countries are not left behind in the structural transformation of Europe.

Interestingly, some of the candidates are performing better than many existing member-states, at least on some of the Lisbon measures. Even if they start from a lower base, our scorecard will reward candidates that show progress and political will. Overall, there are strong reasons why the enlargement of the EU should be good news for the Lisbon strategy:

★ Candidates tend to be fast-growing, dynamic economies. Real GDP growth in the candidates has been consistently higher than in the EU-15. This trend continued through the recent economic downturn.

★ The labour force in candidate countries is often low-cost but highly skilled. Investment into these countries has grown significantly in recent years, in anticipation of their full participation in the single market.

★ Candidate countries have liberalised many industrial and service sectors in order to comply with the *acquis*. Accession countries will, not unreasonably, expect existing members to come into line and do the same.

★ The different economic characteristics of the candidates will help inform policy-making across the EU and present new opportunities for exchange of best practice.

★ Candidate countries have considerable experience of objective benchmarking as part of the accession process. This is a key aspect of Lisbon, even if current member-states have not always treated such exercises seriously. Candidate countries tend to be much more concerned about not 'getting behind' in the accession process, and the Commission's annual reports use this peer pressure to promote reform.

However, these potential positive effects should not distract attention from the possible dangers to the Lisbon process that enlargement could bring. Among the more pessimistic scenarios are the following:

★ The EU after enlargement could become even more unwieldy in its policy-making procedures. A Union of 25 or 27 member-states will find it much harder to agree shared positions on key subjects, especially on the sensitive issue of economic reform.

★ The EU could become introspective after accession, as the reality of absorbing new member-states sinks in. Arguments over the distribution of regional aid and reform of the Common Agricultural Policy could dominate the agenda. But these issues are largely irrelevant to whether the EU achieves its objective of becoming the "world's most dynamic and competitive knowledge-based economy".

★ An extended economic downturn in the current EU that also affected the countries of central and eastern Europe could result in labour unrest and westward migration. Although Europe would probably benefit from increased mobility among its workforce, worries over the impact of such migration could distract rich country policy-makers from the Lisbon agenda. The new member-states would also find it difficult to push through economic reform measures in such an environment.

On balance, however, EU enlargement should reinvigorate the Lisbon agenda. Enlargement should be good news for businesses and consumers, who are the champions of economic reform in both current member-states and the candidates of central and eastern Europe. In any event, the EU needs to address the immediate problem of poor data that hampers meaningful comparisons across the 27 countries. Our analysis has been significantly constrained by this limitation, and future EU policy-making will require much greater investment in pan-European statistical services.

The Lisbon process	C-
Heroes	Sweden, Spain, European Commission
Villains	France, Germany

II The Lisbon agenda

The key elements of the Lisbon summit's comprehensive approach to economic and social policy reform are set out below. For the purposes of the scorecard we have grouped the Lisbon targets under five broad headings.

★ Innovation

The EU cannot compete in a global economy on the basis of low-skilled production in traditional sectors. Europe's record on generating new ideas is strong, but it has had less success in commercialising innovation for the international markets. European businesses still invest too little in new products. The US currently outspends the EU on research and development (R&D) by an astonishing €76 billion every year.

★ Liberalisation

The supposed completion of the EU's single market in December 1992 left much unfinished business. Many barriers to the free movement of goods, services, people and capital remain intact, largely due to the deeply entrenched interests of member-states. The Commission has launched a staggering 1500 infringement cases against member-states for their failure to implement the single market properly. These shortcomings help explain why the economic gains of integration have been much lower than foreseen.

★ Enterprise

New firms are the key to new jobs and innovation. Crucially, Europe lacks a dynamic, entrepreneurial culture in which success is rewarded and failure accommodated. Regulation in Europe, by common consensus, needs to be speeded up, slimmed down and subjected to rigorous impact assessments. Governments should cut state-aids and ensure that protected national champions are exposed to real competition.

★ Social inclusion

Lisbon set out a new approach to European social policy: jobs are the key to social inclusion as well as to sustainable public finances. The EU needs to increase employment levels and improve the quality of the workforce. Concretely, this means that governments should promote investment in skills, increase the mobility of job-seekers, and ensure that the social safety-net does not become a poverty trap.

★ Sustainable development

The EU added sustainable development to the Lisbon strategy at the Göteborg European Council in June 2001. The EU needs to maintain a balance between economic, social and environmental considerations. A competitive and cohesive Europe need not come at the expense of future generations. Investment in 'clean' technologies could produce real economic gains, although in other areas, such as energy taxes, tough choices are unavoidable. But overall, good economic policy remains good social policy – and vice versa.

III The Scorecard

Connection of all schools to the internet by the end of 2001, with training of teachers in the new technologies by 2002 and a new curriculum with a strong IT focus by 2003
On-line access to the main public services by 2003
Adoption of a legal framework for e-commerce by end-2000

A. Innovation

A.1 Information society – Targets:

The EU did not meet the 2001 deadline for connecting all schools to the internet. However, the fact that 90 per cent of schools are now on-line represents a respectable performance. Even when all schools are 'wired up', it will remain a challenge to ensure that every pupil in Europe is taught how to make use of new technology. A solitary PC gathering dust in the headmaster's office does nothing to create an information society, so it is good that the Barcelona summit set a new target of one computer for every 15 pupils by the end of 2003.

More citizens and businesses are getting on-line. Households in the Netherlands, Sweden and Denmark are more likely to be connected to the internet than their American counterparts, but in Greece the proportion is less than 10 per cent – and falling. The Commission's latest benchmarking report on the 'e-Europe' initiative suggests that total EU household connections have recently stalled at around 38 per cent, which is still significantly below US levels.[1] Many Europeans do not have access to a computer, which suggests that moves towards promoting new 'platforms', such as mobile phones and inter-active television, are needed.

Business connections show a similar picture. Almost 90 per cent of EU businesses with more than 10 employees have access to the internet, and 60 per cent have a website. But French companies now lag behind even the Greeks in terms of getting on-line. The collapse of 'dot.com' share prices has held back the growth of e-commerce, and Europe still has some catching up to do: 70 per cent of all internet hosts which process transactions are located in the US, compared to only 20 per cent in the EU.

Europe also needs more high-speed 'broadband' connections to the web. An OECD report in October 2001 found that EU member-states had failed to provide such access at competitive prices. As a result, less than 2 per cent of households in most European countries have broadband, according to Gartner group, an IT research consultancy. Encouragingly, British Telecom announced in February 2002 that it would sharply reduce the cost of broadband, to promote take-up. Germany currently has more such lines than the rest of Europe put together. But Germany achieved this only because Deutsche Telekom is a single, dominant supplier, a position which weakens competition.

The EU still lags behind the US when it comes to overall business investment in information and communications technology (ICT). The European Commission sees this as a major factor in Europe's recent relative economic under-performance, even though the investment gap is starting to close. The most recent data (for 2000) suggest that US businesses invested 5.4 per cent of total GDP in ICT. The UK and Sweden exceeded the US levels but, overall, European businesses invest around one-fifth less in new technology than their American competitors.[2]

The use of IT varies across the candidate countries of central and eastern Europe. But it is generally higher

[1] European Commission, 'e-Europe benchmarking report', 5th February 2002.

than would be expected at their level of economic development. Computer and internet use in Slovenia and Estonia already exceeds that of the 'Club Med' countries in the EU (Greece, Italy, Spain and Portugal).[3] By contrast, Romania and Bulgaria are far behind most other accession countries. Although it is hard to argue they should be spending their meagre resources on internet connections, the emergence of a 'digital divide' in Europe will only accentuate their under-development.

On a more positive note, the e-Europe-plus initiative is an excellent example of how candidate countries are collectively addressing an important aspect of the Lisbon process. Backed by the Commission, the candidates have developed their own programmes of measures that are designed to increase internet access. The initiative's inclusive and collaborative nature, which seeks to highlight best practice, should serve as a model for other areas of the reform agenda. Many current member-states could also learn from the e-government initiatives of Slovenia. For example, citizens there can access a range of public services electronically, and many cabinet meetings take place on-line, ensuring greater transparency and responsiveness to people's concerns.

Information society	C+
Heroes	Netherlands, Sweden, Denmark, Slovenia
Villains	France, Greece, Romania, Bulgaria

A.2 Research and development – Targets:

Establishment of the Community Patent by end-2001
Mapping of R&D centres of excellence, and an Innovation Scorecard by June 2001
Creation of high-speed Trans-European Networks for scientific research by 2001

The dismal failure of the EU to agree on something as basic as the Community Patent casts a shadow over many other achievements in this area. The deadline for a new intellectual property regime – one of the first targets set at Lisbon – was missed. This was due to a long-running dispute over which languages should apply, and a solution still seems far away. As Single Market Commissioner Frits Bolkestein noted in some despair recently: "Ministers once again demonstrated their inflexibility and their inability to put long-term considerations to enhance the competitiveness of Europe before short-term considerations of national pride and protecting the status quo." He put the language controversy into its proper perspective by noting that three-quarters of all patents are already delivered in English.[4]

[2] European Commission, 'The Lisbon Strategy - Making change happen', 15th January 2002.

[3] IFPO, European Commission, 'European Survey of the Information Society', 1999, and World Bank, 'Development Indicators', 2001.

[4] Frits Bolkestein, *Financial Times*, 14th January 2002.

Italy, Spain, Greece and Portugal must rethink their opposition to using only French, English or German, if the Community Patent is to become a cost-effective option for business. If the EU cannot reach an agreement soon, it should follow the suggestion of Swedish Prime Minister Göran Persson. He advocates using the EU's new system of enhanced co-operation, which allows 'coalitions of the willing' to press ahead in some areas where unanimity proves impossible.[5]

The EU has made some progress in joining up its disparate research initiatives. In December 2001, the EU approved an outline for its sixth research 'Framework Programme', which will spend €17.5 billion over the next four years on a range of scientific initiatives. In spite of the deadlock on the Community Patent, the number of new inventions registered by EU researchers is growing steadily. Sweden, Finland and Germany are all on a par with the US or Japan in terms of patent applications per capita. The number of science and technology graduates in the EU is also growing at a comparable pace.[6]

Scientific know-how has always been strong in central Europe and many candidate countries are keen to participate fully in EU research initiatives. The opening-up of these programmes to new researchers could improve their performance and make the much-vaunted 'European Research Area' a reality. The Commission has invested heavily in the GEANT high-speed computer network to join up research institutes across 27 current and future member-states.

Many foreign companies are attracted by the low-cost knowledge base in candidate countries. These firms have also put money into local R&D, notably in Hungary, which offers particular tax incentives for such investment. Slovenia invests the most in R&D as a proportion of national income, and also accounts for the highest number of patent applications per head of population.[7] The Czech Republic invests slightly less than Slovenia overall. But, importantly, private sector investment accounts for a very high proportion of the Czech total, and considerably more as a percentage of GDP than in Spain, Portugal or Greece. However, local firms in many candidate countries are lagging behind in R&D spending. Poland has a huge number of small and medium-sized enterprises (SMEs), but the country's overall spend on R&D is significantly less than 1 per cent of GDP.[8]

The EU as a whole is still failing to turn its leading-edge research into competitive business propositions. European industry must shoulder some of the blame. EU companies are spending only 1.25 per cent of GDP on R&D and risk falling further behind their American and Japanese competitors. Companies in those countries consistently invest more than 2 per cent of their GDP in innovation. The new Barcelona target for R&D expenditure of 3 per cent of GDP by 2010 (two-thirds of which should come from the private sector) is welcome, but challenging. Ministers need a clear strategy for how this will be achieved.

However, Europe's problems are not just about spending more money. The Galileo satellite system is the best example of how some policy-makers, enthused by visionary technology, can lose touch with economic realities. The EU is slated to spend €3 billion on developing this rival satellite service to America's global positioning system (GPS). But it is far from clear how any commercial benefit can result, assuming that the US system continues to be provided for free.

Research and development	C+
Heroes	Sweden, Finland, Germany, Hungary, Slovenia, Czech Republic
Villains	Italy, Spain, Greece, Portugal, Poland

[5] Reported in the *Financial Times*, 27th November 2001.

[6] European Commission, 'The Lisbon Strategy - Making change happen', 15th January 2002.

[7] IFPO, European Commission, 'European Survey of the Information Society', 1999, and World Bank, 'Development Indicators', 2001.

[8] Economist Intelligence Unit data.

B. Liberalisation

B.1 Telecoms – Target:

Liberalisation of telecoms market by 2001, including competitionin the 'local loop' to reduce internet access costs

The previous scorecard acknowledged that the rapid passage of the regulation in December 2000 that unbundled local telephone infrastructure was a real achievement. But there is still a long way to go before consumers feel the positive effects of real competition in this market. On average, EU phone charges are still three times higher than in the US. Even the cheapest charges, in Finland, are almost double the US rates, while the most expensive, in Austria and the UK, are around six times higher.

The EU did make some important progress in 2001 and Erkki Liikanen, the enterprise and information society commissioner, deserves much credit. The European Parliament also endorsed a compromise deal on a new regulatory regime for telecoms in December 2001. This will give the Commission some powers of intervention if it believes that national regulators are failing in their duty to provide a level playing field.

More suppliers are entering the market and prices are falling for long-distance and particularly international calls. But the Commission has had to launch infringement proceedings against Greece, Portugal and Germany for failing to open up their telephone infrastructure effectively. Germany in particular has shielded its dominant supplier, Deutsche Telekom, from full competition.

Most EU regulation will continue to focus on those dominant operators which still retain large market shares. The companies that face more competition will benefit from greater operational freedom. But the Commission's powerful team of competition enforcers, led by Mario Monti, will be watching carefully and have already mounted 'dawn raids' on mobile phone companies believed to be colluding. The EU must promote competition not only within each type of platform (for example, fixed-line, mobile and inter-active television), but also across these different media.

Telecoms are fairly liberalised in the candidate countries. Poland began the privatisation of its telecoms monopoly – Telekomunikacja Polska SA (TPSA) – in 1998, and has opened up local and long-distance markets to competition. New entrants have since gained market share and charges have fallen by around 20 per cent. However, internet access for the Polish population will not increase much until the government tackles TPSA's continuing monopoly of analogue lines. In the other candidate countries, competition has risen significantly owing to the entry of mobile phone companies into the market. Mobile phone use is growing fast in central Europe, allowing some technological 'leap-frogging' to wireless communications. According to the World Bank, Estonia has one of the most modern and socially inclusive communications networks in the world.[9]

Telecoms liberalisation	B-
Heroes	Commission, Finland, Estonia
Villains	Germany, UK, Austria

[9] World Bank, 'A preliminary strategy to develop a knowledge economy in European Union accession countries', January 2002.

B.2 Utilities and transport – Target:

Develop a strategy for completing the internal market for all services by end-2000

In March 2001, the Stockholm European Council set a new target for member-states to make the internal market a reality. Every member-state said they would have implemented 98.5 per cent of the single market legislation by the time of the Barcelona summit. Many countries missed this target, but not by much. Finland, Denmark, Sweden, Netherlands and Spain did their bit. The worst performers are France and Greece, according to the Commission's own 'Internal Market Scoreboard', published in November 2001.

Almost ten years after the 1992 programme was supposed to have completed the EU's single market, 10 per cent of the relevant directives have still not been transposed into law in all member-states. The Commission has launched 1500 infringement cases against member-states for their failure to apply internal market legislation, many of which relate to the cross-border provision of services. France (again), Italy and Germany account for 40 per cent of these cases, but if allowances are made for size, then Ireland, Belgium and Greece are disproportionately culpable.

In many ways, energy liberalisation is the litmus test of the EU's ability to deliver on its Lisbon promises. Currently, only the UK, Finland and Sweden have fully open energy markets. But the Barcelona summit produced some progress in this area, after the French government finally withdrew its long-standing opposition to further energy liberalisation. Business users will be able to choose their suppliers from 2004, with the possibility of full liberalisation soon afterwards. They will account for at least 60 per cent of the total market.

Some candidate countries such as Hungary have already overtaken current member-states in liberalising their energy markets. However, energy costs for consumers in many central and eastern European countries are still too high. Greater inter-connection between national energy networks is needed to make competition work for the benefit of users.

In the transport sector too, poor inter-connections are hampering the creation of a competitive single market. A mere 8 per cent of Europe's freight traffic is transported by rail, sharply down from 21 per cent in 1970.[10] In the supposedly car-obsessed and environmentally irresponsible US, rail freight accounts for an impressive 40 per cent of the total. This dismal European record directly threatens the much-vaunted environmental objectives which the EU set at Göteborg (see separate section below). The Commission has recently announced proposals to bring forward the liberalisation of European rail freight from 2008 to 2006. But France is still hostile, preferring to strike bilateral deals to increase cross-boarder rail freight traffic.

For example, a Franco-German initiative between the French railway company, SNCF, and its German counterpart, Deutsche Bahn, aims to double cross-border freight traffic in five years. This sounds impressive, but such growth comes from a very low base. In spite of their modern railway systems and 300 km long land border, these two countries currently transport more goods to each other by ship than by train. Furthermore, such bilateral deals risk undermining the single market for transport services that the Commission's proposed 'integrated European rail area' is meant to deliver.

In postal services, the EU has made some progress this year, even though many would-be competitors complain that the measures are 'too little and too late'. But the overall policy goal is clear: gradual liberalisation with a view to full competition by 2009.

In public procurement, the picture is more mixed. Purchases by local or national governments account for a whopping 16 per cent of EU GDP. But procurement processes remain opaque and rarely permit firms

[10] European Commission, 'European transport policy for 2010: time to decide', White Paper, January 2002.

from other member-states to bid for government contracts. This disrupts the single market and means that governments and tax-payers are paying over the odds for essential goods and services. Only around one-eighth of public procurement contracts are advertised openly: the UK scores best for transparency, Germany by far the worst.

In terms of overall liberalisation, the candidate countries generally perform well. The Commission's rigorous monitoring of the candidates' implementation of the *acquis communautaire* has ensured that even sensitive sectors such as steel and textiles are now open to competition.

The candidates deserve particular credit for liberalising utilities in the face of consumer opposition. The removal of subsidies is hard to sell politically, because it often means higher consumer prices. Bulgarian households have recently faced a 10 per cent price increase for electricity and central heating, while Hungarian households now spend some 20 per cent of their budgets on energy.[11]

Utility and transport liberalisation	D-
Heroes	Commission, UK, Finland, Denmark, Sweden, Netherlands, Hungary, Estonia
Villains	France, Germany, Greece

B.3 Financial services – Targets:

Financial Services Action Plan to be implemented by 2005
Risk Capital Action Plan to be implemented by 2003

In Lisbon, EU leaders made lowering the cost of capital, through reform of the financial services industry, a key goal. The European Commission's mid-term review of the Financial Services Action Plan (FSAP), published in February 2002, highlighted significant progress towards the achievement of an integrated European capital market. After a year of wrangling, the European Parliament gave a decisive endorsement in January 2002 to the Lamfalussy plan for modernising the regulation of securities markets. The FSAP's target of 2003 for an integrated European securities market is still a tall order, but the EU is making headway – perhaps more so in this area than any other.

Of the FSAP's 42 proposals, the EU has already adopted 25. These include key directives such as those regulating cross-border payments and collective investments in transferable securities (UCITS). The Commission is also asking the member-states and the European Parliament to agree a host of further measures on issues such as market abuse, collateral, distance-selling and accounting standards by mid-2002. Measures on pension funds, conglomerates and prospectuses are slated for agreement by the end of 2002.

[11] European Bank for Reconstruction and Development and EIU data.

These timetables will be challenging. The pensions directive in particular raises thorny tax questions that have thus far defied compromise in the Council of Ministers. The tortured, 12-year saga of the EU's takeover directive, designed to aid cross-border mergers and acquisitions, does not inspire hope. In July 2001, the European Parliament rejected the proposed directive at the last minute, under heavy pressure from the German government. The Commission believes that a new version of the proposal will soon break the impasse. But Germany's continuing hostility, including a determination to prevent companies like Volkswagen falling into foreign hands, does not augur well.

As the leading provider of financial services in the EU, the UK has been pushing particularly hard on this agenda, helped by a sympathetic Spanish presidency. Other member-states such as Ireland realise the importance of competitive financial services to other industry sectors and have backed the liberalisation agenda. The Centre for Economics and Business Research, a consultancy, estimated in December 2001 that €28 billion of European GDP (0.3 per cent of the total) depends on London's financial services industry.

The financial services marketplace is quite dynamic in many candidate countries, thanks to rapid liberalisation and active participation from western companies. The Hungarian banking sector is a good example. Privatisation has brought in foreign investors who have improved the quality of services and compete fiercely for business, to the benefit of consumers.

But in most east European countries, local banks cannot compete with the much greater sophistication and liquidity of western financial institutions. Moody's rating agency reported that the total assets of the top 100 banks in central and eastern Europe totalled just over $200 billion in 1999. This is less than half of the assets of the single largest bank in the UK, France, Germany, Switzerland or the Netherlands. Bulgaria's banking system remains a mess, with the postponement (yet again) of plans for privatisation.

Financial services liberalisation	B-
Heroes	UK, Spain, Ireland, Hungary
Villains	Germany, Bulgaria

C. Enterprise

C.1 Business start-up environment – Target:

Evaluate the business start-up environment in the EU, with indicators on the speed and cost of setting up a new company by end-2000

In January 2002 the Commission finally published its long-overdue study on company start-ups. This showed that, despite some recent improvements, the legal framework for budding entrepreneurs in many member-states is still cumbersome and expensive. Bureaucratic barriers to the creation of new firms have harmful economic consequences. Start-ups consistently generate more jobs and are associated with higher levels of innovation than long-established firms.

On average, European entrepreneurs who want to set up a new company must pay four times as much and wait twelve times as long for legal clearance as their American counterparts. At one extreme, Danish entrepreneurs pay nothing, while Austrian, Greek, Italian and Spanish entrepreneurs pay in excess of €1500. Likewise, new British businesses can be up and running in just seven business days, while their counterparts in Italy and Belgium must typically wait more than six weeks.[12] Enterprise commissioner Erkki Liikanen has called on member-states to act on the results of this benchmarking analysis and, in particular, to promote on-line registration processes.

The 2001 edition of the Global Entrepreneurship Monitor (GEM) highlights the dearth of enterprise in Europe.[13] This study is produced by an international academic consortium and the results show that Europe continues to be the least entrepreneurial region in the developed world. Belgium is, by some distance, the EU's worst performer, while Ireland has improved since the previous year's report to become the continent's most enterprising country. Industrial restructuring in candidate countries has often helped to stimulate an entrepreneurial culture, making a virtue of necessity. Hungary, for example, performs well in the GEM study, coming just behind Ireland, with Poland also scoring well.

A pan-European shift towards a more entrepreneurial society will require the EU to do more than cut red tape. Risk-taking will not become more attractive without long-term cultural change. Finland and Sweden have introduced entrepreneurship into the secondary school curriculum. Educational initiatives are matched with a dynamic venture capital market. Last year, Finland managed a sharp increase in the allocation of early-stage financing to new businesses. But elsewhere, many business leaders believe their own country has a negative perception of enterprise and that high taxes put off many would-be entrepreneurs.

Business start-up environment	D
Heroes	Denmark, UK, Ireland, Hungary, Finland
Villains	Austria, Italy, Belgium

[12] European Commission, 'Benchmarking the administration of business start-ups', Final Report, January 2002.
[13] www.gemconsortium.org

C.2 Regulatory burden – Targets:

Approval of new European Charter for Small and Medium-sized Enterprises (SMEs)
Strategy for simplification of the regulatory environment, including impact assessments, by 2001

The EU should already have agreed on a strategy to simplify its complex rulebook. It has failed to do so. The Commission hopes this might be achieved by June 2002. But many European entrepreneurs remain sceptical that the member-states will grasp this nettle. A Commission survey of 4000 companies suggested that better regulation could produce savings of €50 billion a year. Business leaders rate Finland as the best member-state to do business in, while they name Italy and, surprisingly perhaps, the UK as the most difficult.[14] The UK has championed the cause of cutting red tape and, in fairness, scores well in some other surveys of regulatory burdens, such as the Heritage Foundation's Index of Economic Freedom. On this index, Estonia comes top and France is near the bottom.

The adoption of the SME charter soon after Lisbon has, so far, failed to improve the quality (or reduce the quantity) of rule-making. For example, member-states proposed more than 750 new technical regulations in 2000 – a 25 per cent increase from the previous year.[15] Although regulatory impact assessments are supposedly required in both the EU and the majority of member-states, their effectiveness varies from marginal to meaningless.

The EU has recently produced two reports which suggest new ideas to deal with these problems. The Commission's own White Paper on Governance, released in July 2001, highlighted alternatives to the growth of red tape, such as co-regulation. The Commission defines this as "binding legislative and regulatory action, with actions taken by the actors most concerned, drawing on their practical expertise". For example, the Council of Ministers in November 2001 accepted a 'voluntary agreement' between the Commission and the Association of European Car Manufacturers (ACEA) on measures to improve pedestrian safety.

The second development was the final report of the Mandelkern Group, published in November 2001. This group of senior officials, drawn from all member-states, made a number of concrete suggestions on how to improve rule-making in Europe. The study noted that the costs of regulation in the EU could be in the range of 2 to 5 per cent of GDP – and set out a seven point action plan for reform. These included a number of challenging targets, such as reducing the *acquis communautaire* by 40 per cent by June 2004. At the Barcelona summit, EU leaders endorsed Mandelkern's conclusions.

Candidate countries no doubt wish the EU had thought of this earlier. Adoption of the *acquis* has been an uphill struggle for transition countries from central and eastern Europe. It will be difficult for them to quickly change the focus of rule making to lighter forms of regulation. Many candidate countries also need a more effective advocate for the business viewpoint in government policy-making.

Encouragingly, Poland overhauled its legal framework for business in January 2001, which many in the private sector have welcomed. The government cut back on onerous licensing requirements, thereby facilitating badly needed industrial restructuring. Other countries need to streamline administrative procedures for businesses, enhance minority shareholder rights and protect creditor interests. But political in-fighting delayed implementation of Latvia's new commercial code three times last year, and SMEs still face numerous administrative obstacles in the Czech Republic.

[14] European Commission, 'Internal Market Scoreboard', November 2001.

[15] European Commission, Report on the implementation of the European charter for small enterprises, February 2002.

Regulatory burden	C-
Heroes	Finland, Estonia, Poland
Villains	Italy, France, Latvia, Czech Republic

C.3 State-aids and competition policy – Targets:

Promote competition and reduce the level of state-aids
Strategy for redirection of European Investment Bank / European Investment Fund to support SMEs by end-2000

The Commission's latest state-aid 'scoreboard' shows continuing progress in reducing subsidies to industry which distort the single market. State-aid now accounts for barely 1 per cent of GDP. The UK provides the least support to industry at under 0.4 per cent, while Finland and Portugal give more than three times as much at around 1.3 per cent of GDP. Grumbling from French and German politicians that Commissioner Monti has been overzealous in promoting market forces should be discounted: the convergence of prices across the EU – a key indicator of the effectiveness of competition – appears to be slowing somewhat.

Most central and eastern European countries lack a strong competition culture, and it will take time for their regulators to develop the necessary expertise. But the European Commission and member-state competition authorities are helping out with significant technical assistance programmes. Germany's highly regarded Bundeskartellamt has been at the forefront of efforts to transfer best practice to candidate countries. Nevertheless, many former state-owned enterprises continue to dominate key sectors. All too often, private monopolies have simply replaced public ones.

The Commission has highlighted state-aid controls as a priority area for the candidates. 'Special economic zones' that attract investors through infrastructure grants or tax breaks are a particular concern, since they disrupt the level playing field to which competition policy aspires. There has been some progress nonetheless: the Office for the Protection of Economic Competition, which administers the state-aid regime in the Czech Republic, is now publishing transparent guidance for companies. The agency also co-operated effectively with the Commission's competition officials in a recent case concerning Skoda's operations. In contrast, the state-aid regime in Slovakia is particularly lax and opaque, according to Commission officials. Total subsidies from the Slovak government could amount to as much as 4 per cent of GDP.[16]

State-aid & competition policy	B-
Heroes	UK, Commission, Germany, Czech Republic
Villains	Finland, Portugal, Slovakia

[16] Institute for Management Development, *World Competitiveness Yearbook*, 2001 edition.

D. Social Inclusion

D.1 Bringing people into the workforce – Target:

Employment Action Plans to raise overall workforce participation rates to 70 per cent, those for women to 60 per cent and those for older workers to 50 per cent, by 2010

Getting people off welfare and back into work remains one of Europe's most urgent challenges. Five million new jobs have been created in the EU since Lisbon, the majority going to women. But the EU's 7.7 per cent rate of unemployment is still almost double the US level. It is also much higher than Japan's 5 per cent rate, in spite of that country's decade-long slump.

The overall level of participation in the labour market by those of working age has continued to edge up towards the Lisbon targets, reaching 63.2 per cent in 2001. Sweden, Britain, Denmark and the Netherlands have already achieved the 70 per cent target. Italy, meanwhile, languishes at a disappointing 55 per cent. Last year's Stockholm European Council set intermediate targets for 2005 of 67 per cent (and 57 per cent for women), to maintain momentum.

These goals are probably not achievable without a rapid economic recovery. The downturn has already slowed the pace of job creation, although encouragingly some of the laggards are starting to catch up. Spain and Ireland still managed to increase their overall workforce by more than 3 per cent last year. Greece alone is going backwards.[17] But much greater participation in employment by both women and, especially, workers above 55 years old will be crucial to achieving the overall targets.

The current female employment level in the EU is estimated at 54.7 per cent. In Mediterranean countries, such as Spain and Italy, more women are gradually entering the workforce, albeit from a low base of around 40 per cent participation. Along with Greece, these countries still have much work to do to reach the Lisbon goal of 60 per cent by 2010. Some of the apparent constraints on women working are no doubt cultural, but the Stockholm summit also identified access to adequate childcare as a key issue.

The EU faces an even more severe challenge in keeping older workers in the labour force. Across the EU, only 38 per cent of older workers are active in the labour market – still a long way off the 50 per cent target set at Stockholm. Italy, France, Luxembourg and Belgium employ less than 30 per cent of this age group, wasting a valuable pool of expertise and increasing the burden on their healthcare and pension systems. Austria's rate is a little higher at 34 per cent, but participation of older workers is now falling. Sweden, meanwhile, reaps the benefits of using the skills of two-thirds of this age group.

Generally, the candidate countries have a strong record in job creation, although the transition from command economies has created new pockets of social exclusion. These typically include former workers in state enterprises, those living outside the fast-growing urban areas, and the travelling Roma population. At almost 20 per cent of the workforce, Poland's and Slovakia's unemployment rates are at their highest levels since the fall of communism. The rise in unemployment is related to industrial restructuring, but also reflects inflexible labour markets. The Warsaw government is seeking to address this problem through the 'Belka Plan' of regulatory reform and infrastructure investment, but progress remains slow.

Europe needs more mobility among its workforce, if it is to match supply and demand for labour better. Last year, according to the Commission, only 0.1 per cent of the EU population moved between member-states and only 1.2 per cent moved between regions of the same member-state. American workers are up

[17] European Commission, 'The Lisbon Strategy - Making change happen', 15th January 2002.

to six times more likely to move in search of work. The Barcelona summit endorsed the Commission's ambitious plans to remove obstacles to EU citizens who wish to work in another member-state. Different tax, pension and social security systems can all be major barriers. A new European Health Card will enable EU citizens to receive medical care in other member-states without bureaucratic paperwork.

Bringing people into the workforce	B-
Heroes	Sweden, Spain, Ireland, UK, Denmark
Villains	Italy, Greece, Austria, Slovakia, Belgium

D.2 Upgrading skills – Targets:

A 50 per cent reduction in 18 to 24 year olds with only a basic secondary education by 2010
Foster a culture of lifelong learning, with support from social partners

The latest structural indicators suggest that the EU has made no progress in reducing the number of children leaving school without basic qualifications. More than 150 million Europeans have not completed their secondary education.[18] One-fifth of 18 to 24 year olds are not receiving any further education or training. While the UK has managed to reduce this proportion to 8 per cent, Portugal continues to under-perform badly. Almost half its young people do not receive any formal qualifications. It is hard to see what role they will play in a knowledge-based economy.

The quality of the European workforce therefore leaves much to be desired, and a culture of 'lifelong learning' has hardly taken root. Total adult participation in recognised training schemes is under 10 per cent.[19] But, as usual, there are wide variations within the EU. The UK, Sweden, Denmark, Finland and the Netherlands can all boast participation rates in training of between 17 and 22 per cent. France's miserable rate of around 3 per cent is still falling. Only around one-third of EU workers have ever had computer training for a job, according to the European Commission.[20]

The EU has set up a High Level Task Force on skills and mobility to look into these issues. Its December 2001 report focused on improving the functioning of labour markets by helping workers move more easily between countries and industries. In principle, the use of new technology should help to match supply and demand across the EU. Instead, the dismal picture of labour shortages in some areas and long dole queues in others continues to be the norm.

The OECD publishes the most comprehensive international survey of educational attainment. Its

[18] European Commission, 'The Lisbon Strategy - Making change happen', 15th January 2002.
[19] European Commission, 'The Lisbon Strategy - Making change happen', 15th January 2002.
[20] European Commission, 'e-Europe Benchmarking Report', 5th February 2002.

Programme for International Student Assessment (PISA) finds that European schoolchildren lag behind the world's best in Asia, Canada and Australasia. The study gave top marks to Finland's educational system. But Germany's schools – once seen as a benchmark for quality – perform badly in the OECD's analysis. Wealthy Luxembourg is the EU's poorest performer, behind Russia and Latvia and approaching the performance levels of developing countries such as Mexico and Brazil.

Candidate countries can generally hold their own with current member-states in terms of basic educational attainment. The Czech Republic is below the OECD average on the key indicator of reading literacy, but still ahead of Italy, Germany, Greece and Portugal, as well as fellow candidates Hungary and Poland. Czech students even exceed the OECD average for scientific literacy and so are well-placed to get work in new, technology-driven industries.

Upgrading skills	C-
Heroes	Sweden, Denmark, Finland, Czech Republic, UK
Villains	France, Germany, Greece, Portugal, Luxembourg

D.3 Modernising social protection – Targets:

Agreement of Social Agenda at Nice
Creation of High Level Working Party on Social Protection

Reliable data on social deprivation are hard to find in the EU, let alone in the candidate countries. Within the current member-states, the Commission estimated that 60 million people were "at risk from poverty" in the mid-1990s. Economic growth since then may have reduced the problem, but a prolonged downturn will hit poorest Europeans the hardest.

Each member-state has put forward its own two-year action plan on how it intends to address social exclusion and poverty. This is a good area for the 'open method of co-ordination' to add value. For this to work effectively, the EU as a whole must agree on the key indicators of performance, but then member-states need to implement their own policies to meet those targets. Such an approach allows respect for different social and cultural contexts in each country (including, for example, the role of trade unions). But where some member-states are doing better than others, the laggards should learn from the leaders through the sharing of best practice.

One of the most important conclusions of the Lisbon summit – which EU leaders restated in Barcelona – was that the creation of jobs is among the best ways of tackling social exclusion. In other words, bringing people into the workforce has both economic and social benefits, because those furthest from the labour market are most at risk of marginalisation. One of the biggest barriers to employment is high marginal taxes for lower paid workers, which can perpetuate the poverty trap. Taxes on such workers average 38 per cent across the EU – compared to 28 per cent in the US – and reach 50 per cent in Belgium. Governments must reduce these rates where possible, as the Barcelona conclusions noted.

Long-term unemployment is a good indicator of social exclusion. Encouragingly, the EU is making some progress: 5 per cent of the EU's workforce had been out of a job for 12 months or more in 1995. This rate dropped to 3.6 per cent in 2000, although the most recent data point to a small increase. Spain and Italy suffer from long-term unemployment rates of more than 8 per cent. Moreover, approximately one-eighth of the Dutch working population – around 1 million people – is on generous disability benefits. In fact, the Netherlands has more people on sickness benefits than Germany, which has six times the population. Through a range of active labour market policies, the UK has reduced long-term unemployment to under 1 per cent.

The EU is slowly beginning to address the demographic challenges of an ageing European population. Projections of future pension liabilities are alarming, even if the fiscal effects will stretch beyond current electoral horizons. The financial burden of paying out state pensions could rise by 3 to 5 per cent of GDP in many countries over the next decade.[21] Only fundamental structural reforms to extend the working life of citizens, invest their savings more productively and promote economic growth can make Europe's generous social security systems viable.

Perhaps unsurprisingly, many governments prefer regulatory subterfuge to confronting their electorates with this stark reality. The UK led the charge for welfare reform, despite the fact that its demographic changes are less dramatic and its welfare state is already a relatively small proportion of GDP. But new thinking is spreading across the continent: Sweden and Finland now means-test their pension benefits, while the Polish government unveiled a new pensions system in January 1999, based on a mixture of state investment and private contributions. Hungary and Estonia have made a good start on pension reform. Even Germany has begun to subsidise private pension provision in order to complement its creaking public system, marking an important philosophical shift. Over time, the savings of individual citizens could become a very significant source of new investment capital in Europe.

The debate has therefore begun in earnest across the EU, even if many member-states have yet to embark on meaningful reform. The pressures will intensify: global competition – for capital and skilled labour – is one reason; the euro-zone's tight restrictions on government deficits is another. Many Europeans are justly proud of their systems of social protection, but their leaders have yet to face the challenges of modernisation head on. Further progress is likely once the current electoral cycle is over in the larger member-states, and for this reason we have been generous in our scoring.

Modernising social protection	B-
Heroes	UK, Germany, Poland
Villains	Netherlands, Spain, Italy, Belgium

[21] European Commission, 'The Lisbon Strategy - Making change happen', 15th January 2002.

E. Sustainable development

E.1 Climate change – Targets:

Targets
Reduce greenhouse gas emissions by 8 per cent from 1990 levels by 2010, in line with Kyoto protocol. At least 22 per cent of electricity should come from renewable energy sources
Break the historical link between economic growth and transport volumes ('decoupling'), by prioritising public and environmentally friendly forms of transport

The Göteborg European Council in June 2001 committed the EU to taking its environmental responsibilities seriously. In launching the strategy for sustainable development, the Swedish presidency announced that the economic, social and ecological aspects of all new EU proposals should carry equal weight.

To support this new prioritisation, the European Environment Agency, an EU institution based in Copenhagen, has begun to feed its findings into European Council meetings. Prior to Barcelona, the agency compiled its own assessment of the EU's progress towards achieving its sustainable development objectives. Although the data are patchy and often pre-date Lisbon, broad trends at both EU-level and among member-states are apparent.

Encouragingly, greenhouse gas emissions from EU countries have fallen by 4 per cent since 1990. In Japan and the US, by contrast, they have increased by 6 per cent and 11 per cent respectively. The decline in Europe is mainly due to policy shifts in the UK and Germany, such as their moves towards gas-fired power stations. But the fast-growing economies of Ireland and Spain have increased their emissions by as much as 20 per cent over the same period, and have the most to do to reach their targets.

Electricity production from renewable sources increased by 2.8 per cent over the course of the 1990s. But overall consumption grew by almost as much, so the share accounted for by renewables hardly changed. Without Germany's major contribution, the EU's energy efficiency improved by only 0.3 per cent annually over the last decade. Both an increase in renewable use and improvements in efficiency are essential to maintaining the momentum behind the Kyoto process.

Volumes of traffic also continue to grow in line with the economy, putting additional strains on the public infrastructure as well as the environment. Air travel and road freight, which are particularly damaging, have risen faster than GDP growth, according to the Commission's indicators. The UK produces much more carbon dioxide than equivalent EU economies because of its high car use. But it has recently managed to stabilise these emissions, despite rising economic activity and transport volumes.

Climate change	C
Heroes	Sweden, UK, Germany
Villains	Ireland, Spain

E.2 Natural environment – Targets:

Set new public health targets to reduce particulate and ozone emissions
Improve management of Europe's natural resources. Stop the depletion of biological diversity in the EU by 2010

The Göteborg conclusions stressed that environmental policy must enhance the quality of life of all Europeans directly. A survey of over 200 cities world-wide by Mercer consulting company in March 2002 gave the best environmental scores in the EU to cities in Finland, Sweden and Denmark. Most EU countries have made progress in reducing pollution levels, but they are unlikely to be able to meet the demanding targets set in the newly adopted ozone directive. Urban air quality continues to be very poor in Italy and Greece. Levels of exposure to ozone emissions in these countries are around four times higher than in other member-states.

In terms of natural resources, the Commission's Sixth Environmental Action Programme set the objective of 'de-coupling' the generation of waste from economic growth. European citizens currently throw away, on average, 500 kilogrammes of household waste each year. Depressingly, this figure continues to rise steadily, and the Commission's target of 300 kilogrammes per capita remains far out of reach.

Britain, Ireland and Spain are filling up landfill sites at a faster rate than any other member-state in per capita terms. Recycling is still the exception rather than the norm in these countries. The Common Agricultural Policy and Common Fisheries Policy have been disastrous for Europe's wildlife and delicate eco-systems. Spanish trawlers should take much of the blame for the collapse of fish stocks, for example, while intensive agriculture in southern Spain is also damaging the environment on land.

The candidate countries face an enormous challenge in raising their environmental standards to the high levels rightly demanded by the EU. The Commission estimates that these countries will need to spend €108 to €120 billion over a twenty-year period in order to clean up the catastrophic environmental legacy of communism. These sums dwarf any aid that the EU is providing and could account for up to 2 per cent of the candidates' GDP over the next two decades.[22] Investors who want to take over polluted sites will have to foot part of the bill.

Natural environment	C-
Heroes	Finland, Sweden, Denmark
Villains	Italy, Greece, UK, Ireland, Spain

[22] See Heather Grabbe, *Profiting from EU enlargement*, CER, July 2001.

IV Conclusion

Overall targets

Develop the world's most competitive and dynamic knowledge-based economy by 2010
Ensure average annual economic growth of 3 per cent, leading to the creation of 20 million jobs by 2010

Two years on from Lisbon, the EU seems little closer to meeting its headline goals. The competitiveness gap with the US is still growing: recent figures on GDP per capita suggest that the EU's level is now less than two-thirds that of the US, the widest gap since the 1960s.[23] The latest estimates for economic performance in 2001 suggest EU growth of around 1.6 per cent.[24] Although Commission economists are predicting an upturn in the latter half of 2002, for the year as a whole growth is unlikely to exceed that of 2001. Speaking to MEPs at the beginning of this year, Commission President Romano Prodi put it starkly: "We need to catch up, and catch up fast".

EU businesses, not always allies of the Commission, would certainly endorse that urgency. In its pre-Barcelona submission, the European Round Table of leading industrialists (ERT) stated that progress towards the Lisbon goal is "either too slow or non-existent". The ERT called for closer co-ordination between monetary, fiscal and structural policies and more qualified majority voting on key decisions. The UNICE employers group also stated in its recent report that "tough choices have been avoided ... progress has been inadequate and time is running out".

The optimists are predicting that progress will accelerate after this year's elections in France and Germany. But this is far from certain, for there is not much debate on economic reform in either country. Few leading politicians are emphasising the need for painful structural adjustment, for fear of losing votes. Last year the Portuguese Prime Minister, Antonio Guterres, resigned after disastrous local election results. As the host of the Lisbon summit, he had been one of the key architects of the economic reform agenda.

The Commission's admirably direct 'Synthesis Report' for the Barcelona European Council has highlighted the 'delivery gap' between what leaders promised at Lisbon in 2000 and what has been achieved since then. The Commission is right to argue that "success or failure is largely in the hands of the European Parliament or Council, who must take decisions in key areas of the strategy". Tony Blair said over the summer that the Barcelona Council meeting would be "a real test of our collective European leadership". Our overall score reflects the fact that the EU has come perilously close to failing that test. Barcelona was certainly not a failure, but it is hard to see how it was the "change of gear" that Blair referred to in his post-summit comments.

Summit host and Spanish Prime Minister José María Aznar remains, along with Blair, one of the most enthusiastic advocates of the Lisbon agenda. Italian Prime Minister Silvio Berlusconi, who seems determined to push through labour market reforms and tackle Italy's expensive pension system, is keen to join them. But many on the European left see this Blair-Aznar-Berlusconi alliance as an 'axis of evil', bent on undermining European social systems in favour of American-style 'ultra-liberalism'. The tensions between these differing perspectives were evident in the Barcelona summit's often ambiguous conclusions, and within the domestic debates of most member-states.

Looking ahead, a review of the EU's policy-making cycle could produce some useful procedural changes. Aside from the Lisbon process, member-states are required to submit 'Cardiff' reports on their product

[23] European Commission, 'EU Competitiveness Report 2001', December 2001.

[24] HM Treasury, 'Realising Europe's potential: economic reform in Europe', White Paper, February 2002, and Ifo forecast, January 2002.

markets and 'Luxembourg' reports on their labour markets. The Commission must also produce 'Broad Economic Policy Guidelines' for each member-state and for the EU as a whole. Better integration of these sometimes disjointed processes could help to rebuild momentum. The Commission has promised proposals to this end.

But a more dramatic change to the institutions of European economic policy-making may be necessary to reinvigorate the process of structural reform. Because implementation of the Lisbon agenda is largely a responsibility of the member-states, it falls to the holder of the rotating presidency in the spring of each year to set the agenda and co-ordinate policy across the EU. In spite of the best efforts of the Portuguese, Swedish and Spanish presidencies – all reform-minded governments – progress to date has been extremely slow, as this scorecard demonstrates. The 2003 spring summit will be held under the Greek presidency. But as a consistently poor economic performer, the Athens government may not be best placed to achieve major breakthroughs.

The EU should consider giving greater permanence and profile to the vital work of reforming the European economy. A High Representative for Economic Affairs, appointed by the member-states, could be the answer. This individual would be equivalent in stature and role to Javier Solana, who represents the EU in foreign affairs, another policy area where member-states traditionally guard their prerogatives. Because of his high profile and proven competence, Solana is able to deal directly with foreign ministers and prime ministers in shaping and implementing a coherent EU foreign policy.

The time for a 'Mr (or Ms) Euroland' may soon be at hand.[25] He or she would work at the highest levels to push through economic reforms that are too often derailed by the parochial concerns of middle-ranking ministers and civil servants. Much of his work would be to broker discreet compromises with EU leaders. But where appropriate the new 'Mr Euroland' should also go public, if he believed any EU government or institution was dragging its feet. This would re-energise public debates across Europe. As shown by the recent arguments over the enforcement of the Growth and Stability Pact, the Commission itself simply does not have the credibility to stand up to the big member-states. Only an individual directly appointed by – and answerable to – the European Council could fulfil this role.

The EU should also assign a number of other critical functions to 'Mr Euroland'. He or she should chair the ECOFIN meetings of finance ministers and also the Euro Group, eventually becoming the key interlocutor for the European Central Bank. The post would thereby help to give greater clarity to the EU's fiscal policy. Dissonant voices from 12 or 15 finance ministries are currently sending out conflicting signals. Without clear leadership and direction, the EU finds it hard to make the necessary trade-offs between fiscal and monetary policy. Against this uninspiring institutional backdrop, the weakness of the euro is hardly surprising.

Furthermore, in the G-7 and other high-profile international meetings, the EU has all too often lacked a single, coherent and credible voice on economic policy. A 'Mr Euroland', speaking for the world's largest economy, would have real stature and could engage in discussions with the US Treasury Secretary as an equal partner, something that current EU finance ministers simply cannot do. A 'G-1 plus 6' would be a more accurate description of the current balance of power.

The role of 'Mr Euroland' should go to an individual of global stature, but also someone with a keen appreciation of the dynamics of EU economic policy and a commitment to the Lisbon reform agenda. One strong candidate would be Spanish Prime Minister José María Aznar, who has said he will stand down after the next election in 2004. A key architect of the Lisbon agenda, Aznar has over the last few years cut Spain's unemployment rate in half and achieved economic growth of more than double the EU average. Of course, Spain was starting from a lower economic base, but his experience would be invaluable to the new members of the EU from central and eastern Europe. Aznar's policy of encouraging competition and a flexible regulatory framework has boosted confidence in the Spanish economy, stimulating private sector investment.

[25] See previous CER publications, including Steven Everts, *The impact of the euro on transatlantic relations,* CER, 1999, and Charles Grant, *EU 2010: An optimistic vision of the future,* CER, 2000.

The clouds of economic and political uncertainty may soon lift from Europe. But future historians will deliver an appropriately damning verdict if the EU fails to prepare itself for the long-term demographic and economic challenges that lie ahead. The potential for Europe's success is undiminished. The Lisbon roadmap for integrating economic, social and environmental concerns is clear. However, after Barcelona, it is apparent that Europe's leaders still have much unfinished business to attend to.

Overall assessment of results	C

The CER Barcelona Scorecard

Issue	2002	(2001)	Heroes	Villians
Innovation				
Information society	C+	(B+)	Netherlands, Sweden, Denmark, Slovenia	France, Greece, Romania, Bulgaria
Research & development	C+	(B-)	Sweden, Finland, Germany, Hungary, Slovenia, Czech Republic	Italy, Spain, Greece, Portugal, Poland
Liberalisation				
Telecoms	B-	(B+)	Commission, Finland, Estonia	Germany, UK, Austria
Utilities & transport	D-	(D)	Commission, UK, Finland, Estonia, Sweden, Hungary, Netherlands, Denmark	France, Germany, Greece
Financial services	B-	(C+)	UK, Spain, Ireland, Hungary	Germany, Bulgaria
Enterprise				
Business start-up environment	D	(D)	Denmark, UK, Ireland, Hungary, Finland	Austria, Italy, Belgium
Regulatory burden	C-	(D+)	Finland, Estonia, Poland	Italy, France, Czech Republic, Latvia

State-aid & competition policy	B-	(B+)	UK, Commission, Germany, Czech Republic	Finland, Portugal, Slovakia
Social Inclusion				
Bringing people into workforce	B-	(B-)	Denmark, UK, Ireland, Sweden, Spain	Austria, Italy, Belgium, Greece, Slovakia
Upgrading skills	C-	(D)	Sweden, Denmark, Finland, UK, Czech Republic	France, Germany, Greece, Portugal, Luxembourg
Modernising social protection	B-	(C+)	UK, Germany, Poland	Netherlands, Spain, Italy, Belgium
Sustainable development				
Climate change	C	(N/A)	Sweden, UK, Germany	Ireland, Spain
Natural environment	C-	(N/A)	Finland, Sweden, Denmark	Italy, Greece, UK, Ireland, Spain
Conclusion				
The Lisbon Process	C-	(B+)	Sweden, Spain, Commission	France, Germany
Overall assessment of results	C	(C+)		

KEY: A = very good; B = good; C = satisfactory; D = poor; E = very poor