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Pride and Prejudice

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Pride and Prejudice¹

'A giant stodgy elephant', 'a tortoise that needs to move', 'a sclerotic club of elites', 'a gloomy fortress', 'proud and prejudiced'.....

Inspiring Europe? At best, an uphill task, at worst, an impossible one.

Something has been going wrong with European Union². In an increasingly globalised world, where countries that have historically been burdened with poverty, overpopulation, poor governance are finally emerging out of the bleak corridors of their past, Europe seems to be exploring the abysmal depths of purposelessness, rigidity and stagnancy. Europe seems bewildered by the changing dynamics of the economic landscape and emergence of new competition.

It is disconcerting and amazing at the same time that Europe, a traditional high achiever, finds it difficult to keep up with new trends today. Slow economic progress, rising unemployment, increasing social tensions and inertia stare Europe in her face. Over the past five years, growth in Germany, France and Italy has averaged only 1.6% and unemployment has remained consistently high: 9.3% in Germany, 9.4% in France, 11.2% in Spain.³ Only some countries in the EU, such as Britain, Finland and Ireland, have done well. "But many Europeans believe that they are being *left behind*", reported The Economist.⁴

Europe is currently engaged in two clear kinds of power dynamics. One is the intra-continental ideological divide on socio-economic and political matters between Anglo-Saxon countries like Britain and Ireland and the more Socialist ones like France, Germany and Italy. Different countries within the EU have adopted socio-economic approaches that differ in various proportions. As such, it becomes

¹ Inspired by the title of Jane Austen's famous novel 'Pride and Prejudice'

² For the purpose of this essay, I shall treat 'Europe' and 'European Union' as synonyms.

³ OECD Report. 2005. "OECD urges more dynamic employment policies as response to globalization"

⁴ The Economist, London. 2005. "A Club in need of a new vision: The future of Europe" Retrieved from <http://www.economist.com> on the 16th of January 2006

important to analyze the pros and cons of these differing approaches and understand how Europe can learn from competing practices of its countries.

Another intriguing contest is unfolding between the EU and the developing world like India and China. Compared to the sluggish economic growth of most old EU countries⁵, these relatively new economies in Asia have witnessed a phenomenal growth rate of almost 7-8% in the last year⁶. Beyond the obvious differences like dissimilar stages of economic cycles that Europe and Asia exist in, the important issue to analyze is whether Europe and these emerging economies are simply competitors or is there potential for forging strong partnerships between them.

In this paper, I seek to investigate some of the root problems afflicting European economic growth. Thereafter, I shall analyze how regions within EU, although conflicting in mentalities, can work together to chalk out a blueprint for regenerating their overall competitiveness. Furthermore, I wish to explore how Europe even while competing with the developing world can become an inspiring force for the entire world by truly following its doctrine of 'social justice' in a more global context.

Social Security or A Formula for Complacency?

One of the root problems behind lack of economic reforms can be traced back to European social psyche and political incentives. An oft-cited benefit of democracies like the ones in Europe is that pressing socio-economic concerns among the voters often find their way into timely action by politicians. If indeed the European problem is grave and the average European voter has strong opinions about necessary economic priorities, why are these reforms still elusive? In a seemingly functional democracy, surely, vote-bank pressures should have been sufficient to galvanize politicians into action. But clearly, that is not the case. In spite of knowing that a system of excessively high taxes on capital and labor is incentive-incompatible and leads to unemployment, political parties in France, Germany still advocate "tax harmonization," which is nothing more than a code word for a high tax cartel.⁷ Does this indicate a lack of political judiciousness or is it a more deep-rooted problem?

The answer is a combination of the two. The existence of a comprehensive and wide ranging social-security structure in Europe has reaped significant benefits like

⁵ Please note that this excludes the Nordic countries like Sweden, Finland, Denmark as well as UK and Ireland.

⁶ World Development Indicators. 2005. Retrieved from www.worldbank.org/data on the 15th of January, 2006

⁷ Tupy, Marian. 2003. "Where are you going, Europe?" Cato Institute Journal. Retrieved from <http://www.cato.org> on the 20th January 2006

considerable income security, relatively little poverty and, in some European countries, ample supply of social services. However, these policies which are mainly aimed at 'pain avoidance' have also led to long term *painful* inertia towards economic reforms.

A social security policy often acts like a strong, stubborn safety net in case of an economic downturn. For instance, in case of an unfavorable macroeconomic shock, unemployment benefits help the jobless to a great extent. However, since significant pain is not felt by the voter in the short run, change becomes difficult to attain.⁸ During the 1997 Asian Financial Crisis, countries in SE Asia without a 'total shock absorber' in the form of extensive social security policies felt the pinch. Today, a number of the economic reforms within them have their origin in the lessons learnt from the crisis.⁹

I am not claiming that at a general level, economies that suffer more become better; there are innumerable examples in Africa and Latin America where excruciating economic malaise does not translate into economic well-being. Rather, I am arguing that there are certain unique, systemic issues with the way Social Security arrangements shape social mentality and consequently, the imminence of necessary economic reforms in Europe. The observation by Morgan Stanley, "In the absence of widespread suffering, there is no necessity to change" summarises the endemic problem with the EU¹⁰.

Inspiring Europe must be imminence of reform. Ensuring social justice for the populace is a noble mission and must be continued; however one must be extremely cautious when the cure becomes a deterrent for prevention. Europe needs political conviction not to succumb to overuse of social security to smoothen out economic downturns. If not, this will lead to weakening of the economic fiber as well as shaping unrealistic and unsustainable public expectations.

A Blueprint for Reforms

The next intuitive question is, "What reforms are necessary?" Interestingly, some of the reforms that Europe needs today are fairly intuitive, not rocket science, to say the least.

When faced with increasing competition, while the United States decided to become more productive, EU decided to embark upon a *cartel*. By creating the

⁸ Lindbeck, A., 1995, "Hazardous Welfare-State Dynamics, American Economic Review.

⁹ Mahathir, Mohamad. 1997. Asian Economies: Challenges and Opportunities. Speech given at the World Bank Group - International Monetary Fund Annual Meetings.

¹⁰ Roach, Stephen. 2004. "Europe needs a Stronger Euro". Morgan Stanley Global Economic Forum

"United Fortress of Europe," the European Convention shunned economic and social progress.¹¹

Some nations within the EU like England and Ireland, anticipating the ill-effects of prohibitive labor and environmental standards, high corporate taxes, an unfounded aversion to immigration revised their economic and social policies, yielding valuable lessons. It became evident that economies that adopted anti-immigration policies suffered economic sluggishness while those that invited immigrant workers enjoyed relatively better growth.¹²

Inspiring Europe must be intelligent introspection. I propose that Europe needs a candid introspection of its purpose, future direction and yes, prejudices. Europe should understand that welcoming immigrant workers is neither a zero-sum game, nor a conspiracy to steal jobs. Faced with an acute declining population problem¹³, Europe needs more young workers to provide adequate labor resource to industries and thus, create more wealth and jobs.¹⁴ A sensitive social issue, integration of immigrants into the society is not just an economic necessity; it is a matter of survival.

With growing competition from labor-intensive economies in Asia like China and India, if Europe needs to compete with them in manufacturing sectors, it needs the numbers and the manpower. Rather than be prejudiced against the East European workers, Europe should rejoice at their presence because they are a critical component in fuelling life into the lethargic Old European economy.

Besides implementing immigration policies that recognize economic imperatives, Europe needs to implement a few more essential programs to address this demographic problem. Voluntary extensions of working life, gradual increase in personal pension contribution, more opportunities for women's employment through affordable, usable child-care are some of the innovative strategies that have been implemented in Nordic countries and yielded positive results.¹⁵ Europe should be more appreciative of the best practices in its member countries, give up its misguided pride and adopt them if they indeed prove beneficial. A diverse continent like Europe should learn from itself.

¹¹ Rahn, Richard. 2005. "Europe Vs. Europe". The Washington Times.

¹² Britain had an unemployment rate of only 4.7 percent, even though it absorbed more than 200,000 new workers from Eastern Europe during 2005, while France and Germany had more than 10 percent of their workforce unemployed, despite (or because of) their restrictive work practices.

¹³ The Economist, London. 2003. "Europe's population implosion". Retrieved from <http://www.economist.com/world> on the 14th of January 2006

¹⁴ Friedman, Thomas. 2005. "The World is Flat". Published by Farrar, Straus and Giroux

¹⁵ Lindbeck, Assar. 2003. "Improving the Performance of the European Social Model: The Welfare State over the Life Cycle". Institute for International Economic Studies, Sweden. Retrieved from <http://www.iies.su.se> on 25th of Jan, 2006

Inspiring Europe must be sincere liberalisation. A Europe that wants to stay relevant must also look outwards, towards trade liberalisation. Free trade promises fairer trade rules that have the potential to lift millions out of poverty, bring greater prosperity to EU and its developing partners. Increasingly, it is evident that countries that try to insulate themselves from global changes and tough competition lose significance in the long run. The problem with Europe is that it has been trying to do exactly this!

A strategy of protectionism may work for a short while, but in the long run, it wipes out economies by making them complacent, rigid and uncompetitive. By giving farm subsidies, France is protecting a languishing industry at the cost of inefficient allocation of the taxpayer's valuable money. If EU is serious about its goals of bringing prosperity, it must attack the redundant practice of protectionism. An overly regulatory and reticent approach to the economic challenges posed by India and China who are competing not only in the low value sectors, but also in the hi-tech goods industry might spell doom for European companies.

Collectively EU can use its bargaining position in the WTO to ensure free and fair trade practices, reduce trade barriers with Asia, US and Canada and increase the European consumer's utility by allowing economical but fairly produced imports from the rest of the world.¹⁶ On the supply side, through investments into skills-retraining programs, gradual reduction of agricultural subsidies, inclusion of vocational skills and courses on entrepreneurialism in school and university curriculums, investments in the knowledge based tertiary sector, EU should carve out a place for itself in the evolving economic landscape.

With this new founded supportive political environment, support for corporate and entrepreneurial spirit as well as technological advancement, EU could soon become an attractive hub for companies that want to specialize in the non-tradable goods and services sector.¹⁷ This comparative advantage in non-tradable service-oriented industries is long lasting and difficult to erode.¹⁸ Needless to say, there is competition around, but Europe must endeavor to improve its productivity, compete fair and square and not withdraw into a regional enclave.

Inspiring Europe must be international conscientiousness. In an interconnected world, the impact of one country's policy is hardly limited to itself. Europe must be conscientious in admitting the negative externalities of

¹⁶ Alexander, Douglas. 2005. "Europe in a Global Age". The Foreign Policy Center. Retrieved from www.fco.gov.uk

¹⁷ The Economist, London. 2005. "From Lisbon to Brussels: European economic reforms" Retrieved from <http://www.economist.com/> on the 16th of January 2006

¹⁸ Carbaugh, Robert J. International Economics

its trade distorting policies and should take initiatives to rectify this problem. Trade biasing subsidies in agriculture make it increasingly difficult for poor farmers in Africa, Latin America and Asia to compete fairly with their European counterparts. Inequities in trade play an immense role in exacerbating income inequalities between and within nations.¹⁹ As such, despite the expansion of global trade, too many are being left behind, sometimes inadvertently.

If social justice is indeed dear to Europe, she should not be hypocritical in applying this ethical imperative to only her citizens while denying the same to the developing world. Europe should not abdicate its moral responsibility towards the rest of the world by continuing a vicious cycle of protectionism that entrenches poorer nations in greater poverty. It should allow them an equal opportunity to grow and prosper.

By opening up its markets and following a truly global agenda, Europe can set precedents for the rest of the world and gain incredible moral capital as a continent that has always been sensitive of its surroundings in the past and will continue to be so.

Inspiring Europe must be rigorous demystification. The success of any proposed reform is a function of the agent's credibility and public perception of its benefits. The passionate opposition to the EU Constitution in France and Netherlands indicates that the European Union's image as a prudent supranational entity is a serious grey area. A more candid and open European Union is required, devoid of an overbearing, cryptic personality. This is absolutely crucial to the viability of the above mentioned reforms. An EU that gives consistent public explanation of the purposes, constraints, mechanism, funding, management and potential of the EU will become a more people-oriented and solution-oriented union.²⁰

I wish to highlight that role of media in this context. In a civil society, media has an immense sphere of influence and can shape public opinion through its news. It is unfortunate that in Europe, sometimes the press tends to exaggerate EU's shortcomings and underplay its achievements. For the sake of the common man, it is essential that there is a more objective dissemination of information and the EU combats callous distortions, disinformation or misinformation effectively. Objective and carefully explained information is the key to the success of any economic reform.

¹⁹ The Economist, London. 2005. "Europe's new protectionism" Retrieved from <http://www.economist.com/world> on the 14th of January 2006

²⁰ Alexander, Douglas. 2005. "Europe in a Global Age". The Foreign Policy Center. Retrieved from www.fco.gov.uk

Plural Mentalities, Single Agenda

Strangely enough, the greatest inspiration for Europe is the force of globalization itself - globalization that synthesizes plural perspectives of diverse regions into mutually compatible goals. If Europe responds to globalization with renewed vigor, innovation, enthusiasm and economic agility, it will soon realize that social justice and economic progress constitute a single agenda. A powerful agent of change, a solvent of tradition, globalization presents Europe with a rare opportunity of glory and progress. All Europe needs is - *less pride and lesser prejudice*.