Revitalising Europe’s Economy: Towards Growth

Lorenzo Codogno

Abstract The Europe 2020 Strategy is under mid-term review. This paper looks at the Strategy’s objectives and the means to achieve them, considering the new socio-economic reality that has emerged from the crisis along with new data on employment and social inclusion (or exclusion). It argues that any future strategy should address, at the same time, innovative ways to: (i) enhance potential growth from a lowered post-crisis level; (ii) improve finance for growth given tight budgetary constraints and high levels of public and private debt; and (iii) ensure social and environmental sustainability. The paper contains suggestions for a new approach to Europe 2020 and considers possible structural reforms to enhance growth and employment, compatible with environmental and social goals. Moreover, it discusses the need for some ‘good imbalances’ as by-products of economic and financial integration and includes a few remarks on the current policy mix, which appears suboptimal, and as a necessary ingredient to strengthen the reform process.

1 Introduction

Europe appears on its way to recovery from the worst economic crisis since the Second World War, and maybe even before. The recovery is still weak in some European countries, and especially in the periphery, with domestic demand lagging behind.

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L. Codogno (✉)
London School of Economics and Political Science, London, United Kingdom
e-mail: lorenzo.codogno@tesoro.it

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The crisis made it all the more urgent to launch structural reforms aimed at enhancing potential growth and making national economies more resilient and responsive to the challenges of the global economy(Varga et al. 2013). The ECB now has a firmer commitment to address adverse shocks and can use an expanded arsenal of monetary weapons if deemed necessary. The European Stability Mechanism was established as a safeguard against potential financial market instability.

Although with some initial hesitation, all Member States acknowledged that a monetary union cannot work without a banking union, that is without a single financial market. Now the Single Supervisory Mechanism (SSM) is underway, and the Supervisory Board has already drafted its operating procedures. Member States have reached a political agreement on the Bank Recovery and Resolution Directive, the Deposit Guarantee Schemes Directive, and the Single Resolution Mechanism (SRM), which will provide a Single Resolution Fund as a significant step in the direction of a full-fledged banking union. The ECB is running the Comprehensive Balance Sheet Assessment (BSA) that should strengthen confidence in the soundness of the European banking system.

European institutions and national governments are now better equipped to face systemic shocks. The crisis helped European leaders to make necessary adjustments and strengthen integration, which otherwise would likely not have occurred. Now it is time to shift gears with a renewed strategy for growth and employment.

At the European level, there is already a strategy for smart, sustainable and inclusive growth—Europe 2020—that was adopted in 2010 (European Commission 2010). The Europe 2020 Strategy sets several complementary targets, which were defined so as to promote a growth model based on a multi-dimensional perspective (European Commission 2009). As a model of growth that goes beyond GDP, it was—and still can be—considered at the forefront of policy making design.

In many EU countries, fiscal consolidation has resulted in difficult choices and often investments towards achieving the Europe 2020 targets have suffered. The Strategy itself is under mid-term review, to be completed in 2015 (European Commission 2014). This provides European policy makers with the opportunity to take a hard look—not only at the Strategy's objectives but also at the means to achieve them. This review must consider the new socio-economic reality that is emerging from the crisis, along with new data on employment and social inclusion (or exclusion), as well as future growth prospects.

Any future strategy should address, at the same time, innovative ways to: (i) enhance potential growth from a lowered post-crisis level; (ii) improve finance for growth given tight budgetary constraints and high levels of public and private debt; and (iii) ensure social and environmental sustainability.

This paper contains suggestions for a new approach to Europe 2020 and considers possible structural reforms to enhance growth and employment, compatible with environmental and social goals.

Moreover, it discusses the need for some 'good imbalances' as by-products of economic and financial integration and includes a few remarks on the current policy mix, which appears suboptimal, and as a necessary ingredient to strengthen the reform process.

2 Highlights of the Main Economic Challenges

The European answer to the unprecedented financial and economic crisis focused on the urgency of financial market stabilisation and on fiscal consolidation. Efforts made by the European Union and its Member States to overcome the short-term impact of the crisis and strengthen European governance were remarkable, although somewhat slow and not without mistakes. Significant progress has been made on the issue of financial integration, an important step in the process of strengthening institutions to achieve real economic and monetary union. Most EU Member States will be engaged in fiscal consolidation and/or efforts to reduce macroeconomic imbalances for several years.[1] In this context, policies must focus not only on current account deficits, sovereign debt and the financial sector, but also on productivity and competitiveness to allow the economy to grow out of current problems.

In order to deleverage debt in both the private and public sectors, Member States have adopted several measures which have produced non-negligible adverse near-term effects on economic activity (Varga et al. 2013). In particular, the need to encourage moderate wage developments or even a so-called 'internal devaluation', has had inevitable negative consequences on domestic demand. Sometimes Member States had no other options but to adopt policies that depressed domestic demand over the near term to achieve financial stability and fiscal sustainability. Negative economic dynamics have also contributed to an increase in unemployment and worsening of social conditions, threatening the social viability of such policies.

Emerging from a deep recession, many EU countries find themselves coping with an economic situation characterised by still relatively low growth and high debt, increased poverty, a recovering financial sector and an industrial sector needing a boost in competitiveness and modernisation. Unemployment has reached new heights, particularly among young jobseekers. The consequences of high youth unemployment are destructive, both individually and collectively, through lowered growth potential.

The financial and economic crisis shifted attention to systemic and short-run considerations, to the detriment of medium to long-term policies to support growth and employment. Policies to deal with the social costs of the crisis have lagged further behind. Current policies focused on further fiscal consolidation and additional measures to overcome imbalances, while certainly necessary, do not seem to

[1]In 2014, within the macroeconomic imbalance procedure, in-depth analyses were performed by the Commission for 17 Member States, 14 of which were deemed to be experiencing imbalances of some degree. On the fiscal front, "while the large consolidation efforts over the past years are now bearing fruit […] only two Member States have attained their Medium Term Objectives in terms of structural balance, implying that further consolidation will be necessary." Commission for 17 Member States, 14 of which were deemed to be experiencing imbalances of some degree. On the fiscal front, "while the large consolidation efforts over the past years are now bearing fruit […] only two Member States have attained their Medium Term Objectives in terms of structural balance, implying that further consolidation will be necessary."

be sufficient to the task. With the emergence from the crisis, the focus must accordingly shift to new ways to address the main economic, social and environmental structural challenges facing the EU, to increase growth, jobs, competitiveness and sustainability over the long-term.

3 Overview of the Europe 2020 Strategy

The Europe 2020 strategy is based on the Lisbon Strategy for growth and jobs which was adopted in 2000, renewed in 2005 and still in place up to 2010 (European Commission 2005). The current Strategy outlines "a vision of Europe's social market economy for the 21st century" aimed to "turn the EU into a smart, sustainable and inclusive economy delivering high levels of employment, productivity and social cohesion". Europe 2020 is an effort based on three mutually reinforcing attributes for growth: (1) smart, through investments in education, research and innovation; (2) sustainable, through a move towards a low-carbon economy; and (3) inclusive, by emphasising job creation and poverty reduction.

The Strategy sets out five interrelated and exemplary headline targets intended to be "representative", but not exhaustive, of the EU priorities in the areas of employment, R&D, climate change and energy, education and the fight against poverty and social exclusion.[2] The Strategy also sets out seven flagship initiatives at the EU level that include specific work programmes in important areas for growth (skills and jobs, youth, innovation, digital agenda, industrial policy, resource efficiency, fight against poverty and social exclusion). National targets reflect the different starting points and capacities of individual Member States.

The Europe 2020 strategy was intended to be the medium- to long-term growth strategy in the EU, but almost five years since its launch it is still far from delivering its objectives (European Commission 2014). It was also the starting point for the European semester that has become the overall framework for coordination and convergence of Member States' policies, and is the building block from which a revised strategy can be designed.

4 Assessment of Europe 2020

The Commission notes the "mixed progress" in achieving the Europe 2020 goals (European Commission 2014) (see Table 1 in the Appendix), but a review of the progress on each target shows a somewhat less optimistic assessment of performance, with only the climate change and energy indicators likely to be reached given current efforts and slower growth. Indeed, we should acknowledge that the

[2] For a discussion about targets see Codogno et al. (2009).

climate change and energy targets are binding, given that they were defined on the basis of a legal framework at both the EU and the Member State level.

The protracted economic crisis has played a major role in hampering the progress towards the achievement of other Europe 2020 targets. Even in cases in which there seems to be progress, the situation may in reality be less clear cut. For example, the seemingly satisfactory progress in reducing the drop out and educational attainment rates is attributable in large part to increased demand for education, as a result of the reduction in employment opportunities that might otherwise encourage would-be students to enter the workforce. To some extent the crisis has even helped Member States move closer to reaching climate change and energy targets, given lower production (and thus CO_2 emissions) and lower overall energy demand. Moreover, achieving targets may not necessarily make the ultimate goal of sustainable, smart and inclusive growth any closer as the relationship between targets and the ultimate policy goal is rather loose.

At any rate, the most worrisome performances are those towards the social targets, with an expected failure to reach the employment target and an increase in the population facing poverty and social exclusion. The current at-risk-of-poverty indicator may underestimate the social costs of the crisis, as this category is defined to include those earning below 60 % of median income. As median incomes fell during the crisis, the poverty line automatically shifted downward as well.

The crisis has also meant falling resources dedicated to research and innovation. While immediate fiscal consolidation warranted spending cuts, the consequences of reduced R&D investments may manifest themselves in the long term via lowered innovative capacity and slower rates of potential growth. Moreover, the fragmentation of markets has exacerbated the crisis at the time major restructuring efforts were underway in many countries to respond to the challenge of globalisation.

There is thus a need to assess how to strengthen and realign the strategy to make growth, employment, productivity and social cohesion again the top policy priority. The Commission's stocktaking Communication is a good starting point, but further analysis and debate will be needed to develop the EU's post-crisis growth strategy for the 2015–2020 period and beyond.

Implementation of the Strategy in the past years has revealed a number of weaknesses that need to be tackled. While policy priorities have changed as a result of the new economic conditions, the methods and overall approach to structural reforms have only slightly changed since the Lisbon Strategy. Additionally, the incentives for Member States to effectively reach the proposed targets have in some cases progressively weakened, while in others the budgetary means—both at the national and the EU level—are not sufficient.

To make the Europe 2020 Strategy more effective, greater ownership by Member States is needed, in particular by strengthening peer interest and pressure. At the same time, the European dimension needs to be reinforced. It is evident that, partly because of the economic crisis, governments tend to focus mostly on the implementation of their own reforms and recommendations. Attention to the EU-wide framework by individual Member States (and also by EU institutions) has been insufficient, particularly given the potentially positive spill-over effects of reforms by other EU countries. Moreover, there are reforms that are strictly competence of the Union, such as the strengthening of the Single Market for goods and services. Overall, evidence from Member States reveals that the governance structure of the Strategy has not necessarily led to an alignment between national policies and EU objectives.

While it is clear that the achievement of the Europe 2020 targets would benefit all EU countries, these potential benefits have not been emphasised, nor have the overall benefits of reaching the Europe 2020 targets been properly estimated at EU level. The Europe 2020 Strategy ignores the integration and regulation of financial markets and does not directly incorporate Single Market considerations. Moreover, the recommendations in the context of the Europe 2020 Strategy have not been adequately tailored to needs of each individual Member State.

5 Suggestions for a New Approach to Europe 2020

The overarching goal of the Europe 2020 Strategy is the creation of favourable conditions to raise the growth potential of the Member States and therefore it is of the utmost importance giving credible signals to create and strengthen expectations of future growth and prosperity. The Commission has launched an EU-wide public consultation of stakeholders on the review of the Europe 2020 Strategy. It will then propose revisions to the Strategy by early 2015 taking into account the results of the public consultation and the discussion in technical committees.

While acknowledging that the economic crisis has limited the capacity of the EU collectively and of each individual Member State to achieve Europe 2020 targets, the current situation calls for renewed efforts by Member States and the EU as a whole to implement structural reforms focusing on strengthening productivity and competitiveness to enhance growth and employment.

This would require, among other things, greater accountability of Member States through strengthened peer pressure and benchmarking of policies. The European Semester, which initially focused on the objectives and targets of the EU growth strategy (and related bottlenecks), has become the forum to enforce governance procedures related to the Stability and Growth Pact and, more recently, the Macroeconomic Imbalances Procedure due to the crisis. As a result, attention to growth, other than national fiscal concerns, has been greatly reduced. The rebalancing of EU priorities towards growth and employment may thus require a rebalancing of the European Semester as well. Indeed, the review, to begin later this year, of governance structures related to the so-called Six Pack and Two Pack should reinforce the central role of the Europe 2020 Strategy.

The review of Europe 2020 must consider the current status and validity of targets, the role of, and possible successors to, flagship initiatives, as well as ways to improve the governance of the Strategy (Codogno et al. 2009). In doing so, the consequences of the crisis must be duly taken into account. Communications should be made more effective and easily accessible to all stakeholders, including the general public that often associates the EU with fiscal constraints but not necessarily with greater growth and employment opportunities.

More attention than in the past should be dedicated to those targets that have become increasingly difficult to reach, namely employment and social inclusion targets, to put in place the means by which they can be met. Other objectives regarding research and innovation, as well as education attainment, will also be difficult to meet in a number of Member States. Accordingly, there may be room for not only prioritising, but also redesigning the applicable flagship initiatives to provide greater support at the EU level towards meeting these goals. Headline targets simply represent the direction to follow but they can, by no means, be considered comprehensive. They should be complemented by a much broader set of indicators, some of which highly complementary while others would require some trade-offs (Codogno et al. 2009).

The 2015 mid-term review of Europe 2020 provides an opportunity to institutionalise and formalise an increased emphasis on growth and employment by making it the core of the EU growth agenda. More specifically, it could elevate employment to an overarching priority, not solely through labour market policies, but rather more broadly through employment-friendly policies, defined as policies that create the necessary conditions for generating employment opportunities. For instance, improving SME access to credit would allow additional investments and generate growth and jobs.

A new Europe 2020 Strategy with employment-friendly growth policies as the top priority would provide Member States with a mandate to focus on the most beneficial reforms, while avoiding extraneous or ancillary initiatives. High unemployment and inactivity, particularly among the youth, is one of the most serious challenges now facing the EU. The competitiveness of EU economies, the future prosperity of its society and the sustainability of its welfare systems rest upon the participation and productivity of the labour force.

In order to trigger positive expectations for improved growth, more resolute structural reforms at the national level are, of course, needed. For national reforms to be effective, however, they must be implemented in a supportive macroeconomic environment of stronger aggregate demand and confidence, which also means confidence in the future of the Union (Padoan 2012a, b). Against this backdrop, the debate should also focus on what can be done to rebuild a positive relationship between the Union and its citizens and rebuild a strong sense of common purpose. This would call for further deepening of the Union.

Following such an unprecedented shock and the resulting structural policy response, the European economy and society must deepen integration with speed and conviction. The risk of multiple equilibria is still looming, and if it materialises, it would bring to an end the European project. European governments could accept the current stabilisation in financial markets and the structural reforms completed so far, abandoning more ambitious programmes to foster economic growth and integration. At the current juncture, it is vital to link the short term with the long term in order to jump on a different development path, which would lead to a better equilibrium. Achieving smart, sustainable and inclusive growth does not imply just a one-time choice, but requires a coherent and shared long-run commitment.

The alternative is instead years and years of subdued growth, with increasing imbalances and divergence among Member States and with progressive weakening of the role of Europe in the global political and economic arena. Policy makers need to revive a vision of the future of the Union, where common institutions and decision making are perceived as engines of prosperity and not as obstacles, or worse, as constraints on well-being.

6 Deepening the EU Single Market for Services, Networks and the Digital Economy

Coherent with this vision is the deepening of the Single market, particularly in services, networks and the digital economy, as these are the areas that would, by all analyses, greatly improve growth potential and increase employment opportunities (Monti 2010). The EU Single Market is not directly contemplated in the Europe 2020 targets and initiatives (with one exception being the Digital Agenda flagship). Rather, the single market is considered as a ‘tool’ that can promote the objectives of Europe 2020 and integrate existing initiatives.

A strengthening of the internal market would generate greater economic growth and produce more employment opportunities. Its exclusion from Europe 2020 appears therefore to be a glaring omission that could undermine the entire framework. Furthermore, the strengthening of the internal market would facilitate a greater integration of EU industries within global value chains. Indeed, a greater presence in these value chains is possible only if markets for products and services are open and interconnected, investment in research and innovation is fostered and a suitably qualified workforce is available.

Given the significant benefits to be derived from fully implementing the Services Directive, furthering the integration of services should be incorporated into Europe 2020. The Commission has analysed individual services and professions to assess the implementation of the Services Directive. On technical ground, it is already possible to launch specific initiatives in sectors that offer the highest potential.

More specifically, the Single Digital Market is also an area to be included in Europe 2020. Currently, the Digital Agenda is only included as a headline initiative under the Smart Growth priority. Given the expanded role of the digital economy since the original Europe 2020, this could potentially be elevated among Europe 2020 main priorities. Alternatively, the Digital Agenda initiative could be expanded to become part of a broader initiative to integrate markets in network industries.

The EU published the first Transport Scorecard in April 2014 to compare member-state performance. Similar to the Single Market Scorecard, these indicators capture compliance with EU directives as well as provide a snapshot of transport integration. Such integration indicators should be applied also in other areas in order to accelerate progress towards fully integrated network industries.

Moreover, although renewable energy is included as one of the environmental targets in Europe 2020, oddly the integration of energy markets is not part of

Europe 2020. Given the time required to fully integrate energy markets and the importance of energy security, this could be a good candidate for inclusion.

To sum up, many important areas instrumental in stimulating potential growth are noticeable for their absence from the current version of the Europe 2020 strategy.

7 Finance for Growth

A 'Finance for growth' initiative, launched at the EU and national level, could decisively eliminate financial market fragmentation and create a favourable conditions for longer term investment.

The ultimate objective is having single financial and capital markets where economic agents can make investment choices without unjustified credit constraints: credit should be allocated competitively, irrespective of location/nationality, based entirely on the borrowers' capacity to produce wealth and cash flows upon which credit can be safely repaid. This is the best way to ensure that productive projects, including long-term ones, can be effectively pursued while protecting savers and investors. Of course this requires an integrated and effective financial system involving both the private sector, through financial markets and intermediaries, and the public sector, through supervisors and regulators.

The progress made in the past towards integration has been impressive, not only driven by the introduction of a common currency but in reaction to the global financial crisis. The creation of a Banking Union is the most visible and recent achievement, although starting from a situation of dis-integration following the financial crisis.

Now that the major reforms for the banking sector are about to be completed, there is a need to increase efforts to further develop and integrate EU non-bank finance, including long-term institutional investment and direct capital markets. Promoting further progress must focus on the need to ensure ample availability of credit to small and medium enterprises, which are the backbone of the European economy. The global financial crisis has highlighted that the 'regime shift' to a new risk-adverse steady state in the financial system is particularly challenging for otherwise creditworthy SMEs.

There is plenty of room for European initiatives in the area of research, innovation, human capital development, green economy, energy, transport and digitalisation. Recently the need for financing long-term investment projects are also related to new areas of development such as health care services, full information-technology integration among different level of government and the EU, network systems in the energy and communication fields and a new effort on the digital agenda. They are all areas of potential growth that require private and public capital for their development. Refocusing the EU budget could be a source of financing for these initiatives as well as the set-up of a European infrastructure fund and the recapitalisation of the European Investment Bank.

8 Greening of Growth

The recent economic crisis has provided an opportunity for Member States to define policies aimed at promoting the transition to a ‘green economy’. A strategic vision, in this sense, would require that policies to overcome the crisis are environmentally sustainable.

In this sense, green growth can be a tool to achieve economic growth while preventing environmental degradation, biodiversity loss and the unsustainable use of natural resources. To facilitate the transition to this idea of economic growth it is necessary to explore all opportunities. Therefore, it is crucial to have data and indicators that appropriately measure progress towards ‘green growth’.

The aim would be to promote a better use of natural capital, through a mix of policies that internalise environmental externalities, and to emphasise certain strategic productive sectors, such as agriculture, food, tourism, services with high value added and employment potential, as well as the industrial system as a whole.

The full incorporation of policies oriented to green growth into the Europe 2020 strategy can create new business opportunities and increase the competitiveness of enterprises, reducing the cost of energy and the exposure of the economy to fluctuations in energy prices. Among the sectors with the most potential are the upgrading of energy efficiency of buildings, the efficient management of water sources and waste, activities related to adaptation to climate change and the development of renewable energy sources.

‘Green growth’ cannot be promoted in isolation from other public policies, but must be part of a broader strategy addressing both supply and demand. It must become an essential element in production dynamics and the behaviour of businesses and individuals. In this sense, it must also be tailored to national circumstances.

Green growth can be promoted through: (i) a change in the composition of taxes, in particular through a well-designed increase in environmental taxes and a corresponding decrease in income taxes; (ii) the creation of long-term price signals through economic instruments, putting a price on externalities and applying the principle of ‘polluter pays’, providing strong indications to the market in terms of investment opportunities; (iii) the focus on sustainability of growth to prevent an eventual reduction in the growth rate once the limits of natural resources are reached.

9 Imbalances Versus Integration

In general, policies to correct imbalances can reduce macroeconomic risks related to these imbalances, thus fostering better economic conditions. The same holds true for excessive fiscal imbalances. Fiscal adjustment becomes the precondition for future economic growth. There is nevertheless a thin line between addressing economic imbalances on the one hand and damaging potential growth or undermining social cohesion and sustainability on the other. The quality and composition of the response to imbalances becomes pivotal. Measures to correct external and internal macroeconomic imbalances, as well as excessive fiscal imbalances, should draw from the improved economic outlook to encourage growth and convergence to a greater extent than past practices.

In a context of economic integration, divergent patterns of sectoral specialisation enhance economic growth but also contribute to produce divergent productivity growth rates and current account balances, implying co-existence of different industrial and economic structures and a different pace of employment creation and output generation in different countries. In the long run, the literature suggests that sectoral composition also has a substantial impact on TFP growth. Moreover, greater specialisation could result in a de-synchronisation of business cycles across countries and non-synchronous reactions to common shocks within the economies of the market union, which would have ultimately to be offset by fiscal policy.

The benefits of specialisation would be evident for a currency union, in terms of productivity growth and competitive advantage, and would not make the whole-area economy weaker. Imbalances, to some extent, could be considered as a by-product of integration.

The crisis urged decisive action to prevent the collapse of the European Economic and Monetary Union. Country-specific imbalances (especially fiscal and trade) are often pointed out as being prominent sources of problems within the Euro Area. While imbalances are certainly at the root of the current crisis, we must also acknowledge that the economic recipes currently proposed to reduce imbalances do not fully consider the economic effects of increased market integration and specialisation. For the above reasons, different growth rates and output trends across Member States, within certain limits, should be expected as a result of greater product and services market integration (Codogno 2011a, b).

In other words, there are also 'good imbalances' that reflect increased economic integration and product market specialisation, together with greater financial and banking integration.

10 Finding the Appropriate Policy Mix

The key for EU economic success lays on structural supply-side measures, which may sometimes have negative effects on aggregate demand over the near term. Moreover, private and public sector deleveraging must continue. In this situation, tight fiscal policy and insufficiently accommodative monetary policy/fiscal fragmentation may leads to:

(i) Weakness in consumer spending.
(ii) Insufficient recovery in investment activity.
(iii) Uncomfortably high unemployment.
(iv) Continuing disinflation (and risks of deflation).
(v) Rising Euro Area C/A surpluses.

(vi) Strengthening of the euro exchange rate.
(vii) More problematic debt dynamics.

In the Euro Area there is evidence of all these phenomena, and thus there is a need to combine structural policies with an appropriate policy mix over the near-term to facilitate the transition towards higher potential growth. The above mentioned phenomena (Fig. 1, 2, 3, 4, 5, 6, 7, 8, 9 and 10 presented in the appendix) seems to suggest that the current policy mix is suboptimal and is not facilitating the reform process.

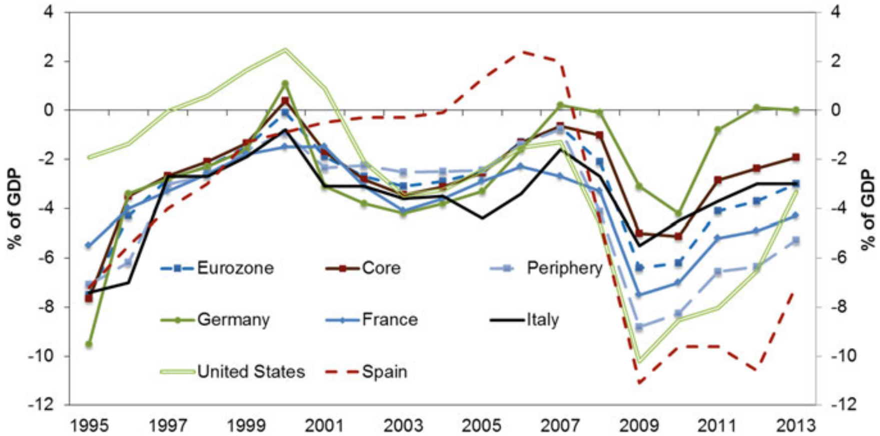

Fig. 1 Additional fiscal consolidation is unavoidable. *Note* Deficit data Greece, included in Pheriphery, are not available for the period 1995–1999. *Source* Eurostat, US Department of the Treasury, Bureau of Economic Analysis

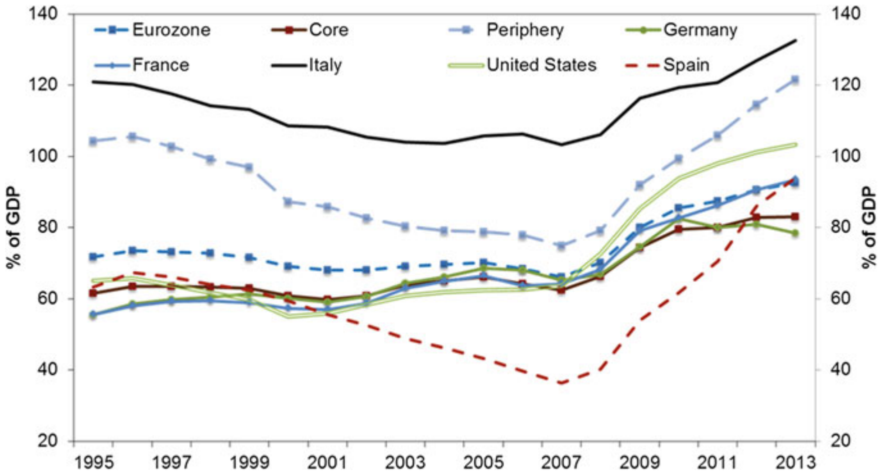

Fig. 2 Public debt deleveraging has yet to start. *Source* Eurostat, US Department of the Treasury, Bureau of Economic Analysis

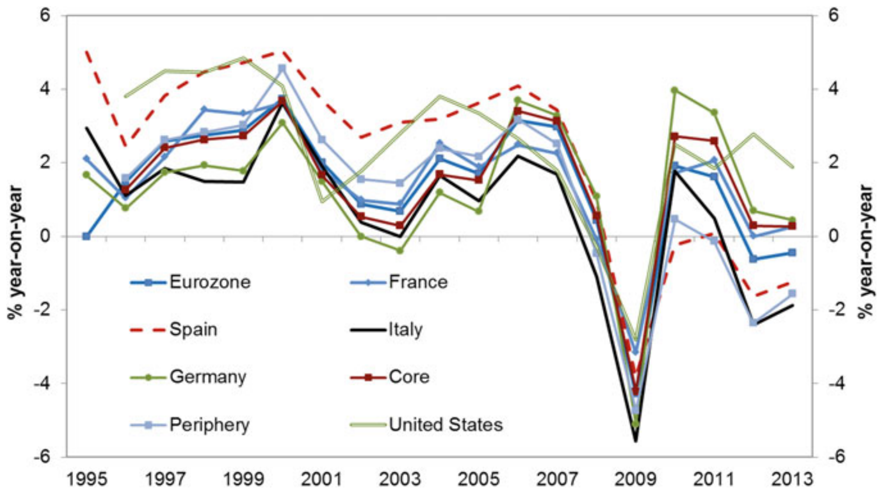

Fig. 3 Is GDP going back to its pre-crisis potential? *Source* Eurostat, BEA

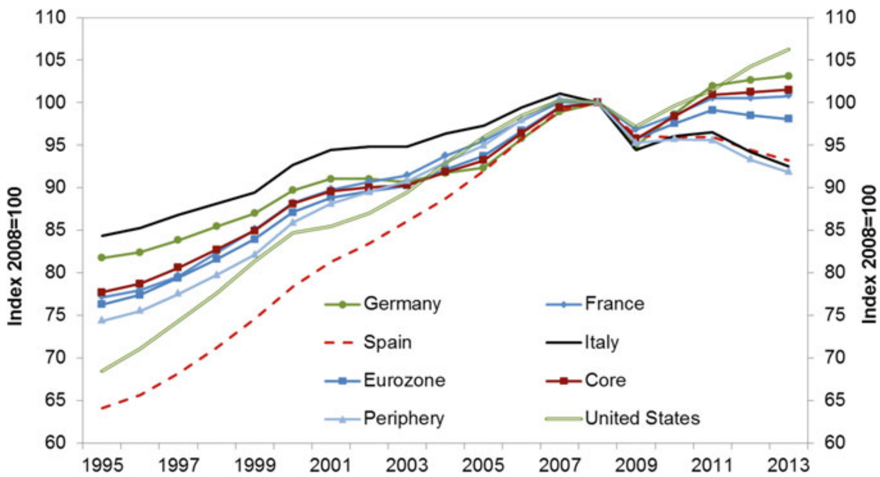

Fig. 4 Are GDP level losses going to be recovered? *Source* Eurostat, BEA

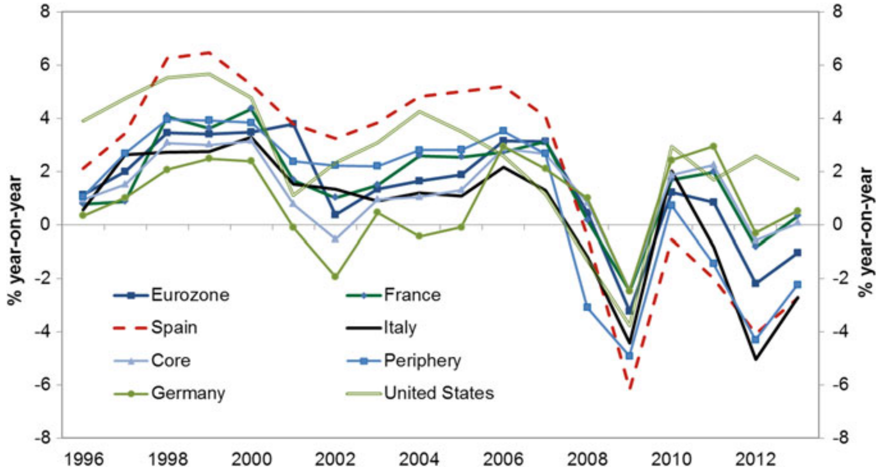

Fig. 5 Domestic demand improving slowly even in core EA countries. *Source* Eurostat, Oxford Economics

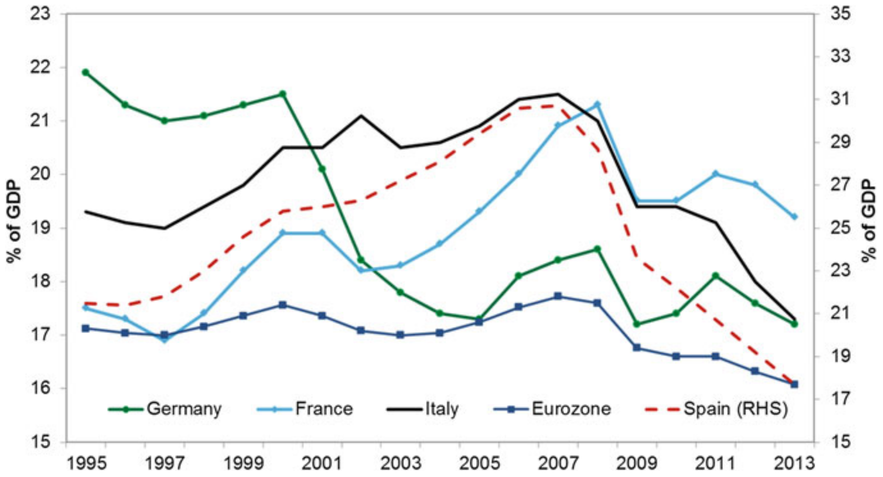

Fig. 6 Investments for growth: the challenge to reverse current trends. *Source* Eurostat

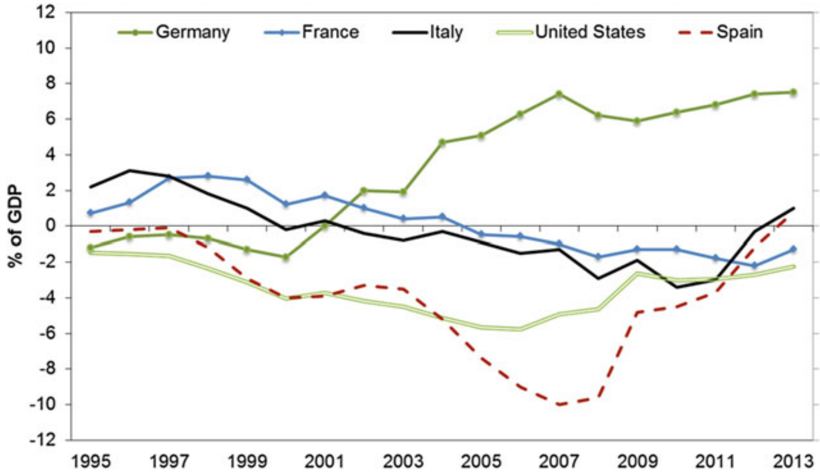

Fig. 7 Policy mix leading to current account surpluses. *Source* Eurostat, ECB, IMF

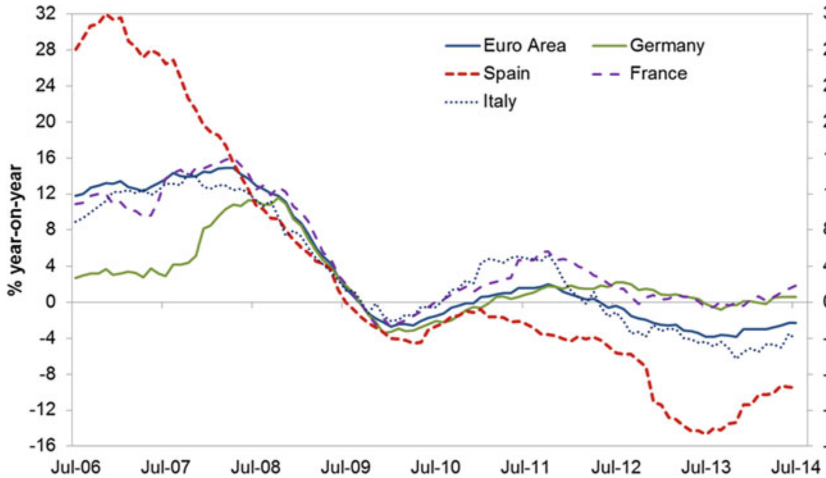

Fig. 8 Contraction in credit growth: still no turning point. *Source* ECB

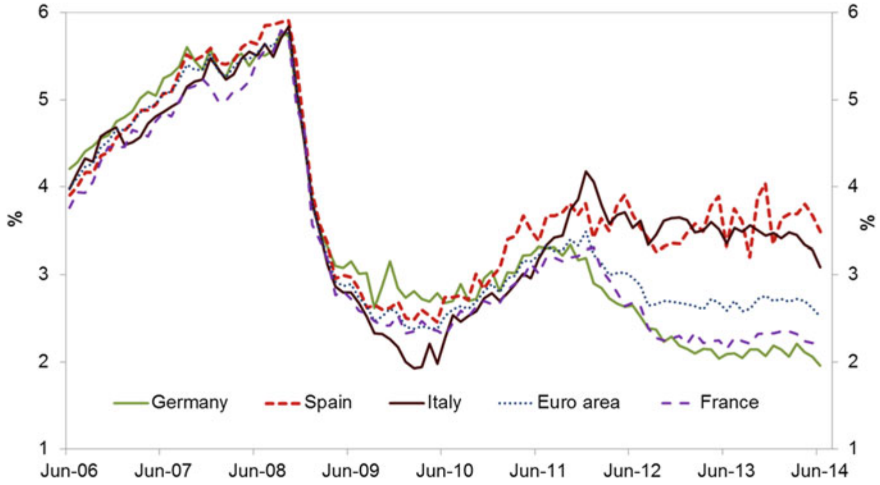

Fig. 9 Cost of credit: the gap among Euro Area countries remains wide. *Source* ECB

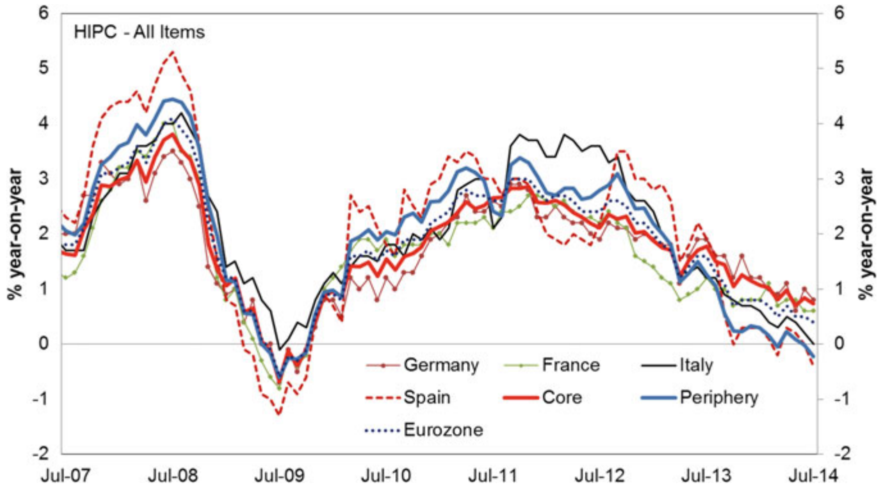

Fig. 10 Disinflation continues (with non-negligible risk of deflation). *Source* ECB

11 Conclusions

The pre-crisis paradigm was unsustainable, economically, socially and environmentally, and Europe needs a new vision of well-being that recognises new challenges, new opportunities and new sources of growth.

A renewed focus on promoting growth should take into account areas such as the efficient functioning of the labour market, addressing issues such as the skill mismatch (for example, by redefining a flagship such as "an agenda for new skills and jobs"), areas related to the strengthening of the single market, increasing the integration of financial markets (i.e. banking union) and policies to promote a transition to a 'green economy'.

Inequality has increased in many European countries in recent years. In order to make the recovery sound and sustainable, policies must boost long-run GDP growth and reduce inequality as well. Investing in education and skills, promoting the integration of immigrants and helping more women into decent employment, are just a few examples of such policies.

But it is not only revisions to its content that would provide added momentum to the Strategy. For Europe, complete recovery is not a return to normality; there is a need to foster new sources of growth and competitiveness, based on knowledge-intensive activities, high productivity and environmental sustainability. The new vision must be rooted in the medium to long run. The review of the Europe 2020 strategy is an important opportunity in this sense.

Europe has learnt some lessons from the crisis. Inter-connectedness touch on every dimension of Europe's economic and social lives, so that nationally-oriented policies proved to be not only ineffective, but made the imbalances worse. It follows that national imbalances cannot be corrected only by means of asymmetric mechanisms, particularly those that place the entire burden of adjustments on a few countries. Indeed, experience shows that such asymmetry jeopardises growth and even social cohesion in the adjusting countries and also risks spreading the slowdown to other countries. Only well-coordinated policies will be successful in achieving further integration and enhancing potential growth for the whole area.

Sufficient leeway must be allowed for imbalances that are necessary to make an efficient allocation of factors of production and financial resources within Europe.

Finally, to help this process, some rebalancing of the current policy mix may be desirable to maintain price stability, prevent further increases in the Euro Area current account surplus, discourage further appreciation of the euro exchange rate, facilitate deleveraging and, finally, provide some near-term support to demand to strengthen the economic recovery and the citizens' support to much-needed reforms.

Appendix

Europe 2020 Background (Table 1).

Table 1 Summary of Italy's key results on Europe 2020 targets

Target	Flagship	EU-wide status (2012)	Expected EU-wide status (2020)	IT status (2012)
Employment: at least 75 % of working age population (ages 20–64) *IT Target*: 67–69 %	Innovation union Digital agenda for Europe Youth on the move Agenda for new skills and jobs	**68.40 %**	**Expected 72 % (74 % if national targets met)**	61 %
Investments in R&D: 3 % of GDP *IT Target*: 1.53 %		**2.06 %**	**2.6 % at best**	1.27 %
School drop-out rates (<10 %); **Completing tertiary education** (at least 40 % of 30–34 year olds) *IT Targets*: **Drop-out rate**: 16 % **University graduates**: 26–27 %		**Drop-out rate**: 12.7 % **University graduates**: 35.7 %	**Drop-out rate**: "Target Broadly Achievable" **University graduates**: "Target Likely to be met"	Drop-out rate: 17.6 % University graduates: 21.7 %
Reducing GHG (by 20 or 30 % "if conditions are right"); **Increased Renewables Share** (to 20 %) **Energy Efficiency** (+20 %) **IT Targets**: **GHG**: −13 % **Renewables**: 17 % **Energy Efficiency**: 158.0 mTOE	Resource-efficient Europe An industrial policy for the globalisation era	**GHG reduced by 18 %** **Renewables**: 14.4 % **Energy Efficiency**: primary consumption fell; energy intensity increased	**GHG**: −24 % **Renewables**: 21 % **Energy Efficiency**: on target (not specified)	GHG: −4.7 % Renewables: 13.5 % Energy Efficiency: 155.2 mTOE
Poverty and Social Exclusion: 20 million lifted from at-risk group *IT Target*: **Poverty reduced by 2.2 m**	European platform against poverty	**Increased from 2009**: 114 million to 124 million	No evidence of a "quick-fix solution"	Poverty *increased* by 3.4 million (from 14.8 m in 2010 to 18.2 m)

In addition to the summary provided in the Stocktaking Communication, Eurostat prepares an annual report on Europe 2020 progress. http://epp.eurostat.ec.europa.eu/cache/ITY_OFFPUB/KS-02-13-238/EN/KS-02-13-238-EN.PDF

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