# THE LISBON STRATEGY AT MID-TERM: PRESENT ACHIEVEMENTS AND FURTHER EXPECTATIONS

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***Abstract:*** *Directing European economies to new paths of development by closing the economic gap between Europe and the Unites States and advancing ahead of the USA until 2010, was the backbone of the Lisbon Strategy's success, launched by the EU in 2000. This Strategy was designed to increase the growth and modernize Europe, while caring for sustainable development and social cohesion.*

In March 2000, at the outset of their Summit in Lisbon, leaders of the European Union[1] pledged to transform the EU into the "*most dynamic and competitive knowledge-based economy in the world*" by 2010.

The Lisbon Strategy was designed to increase the growth and modernize Europe, while caring for sustainable development and social cohesion. The Strategy represented an innovative approach to development because economic objectives were not juxtaposed with social ones. Instead, the Strategy endeavored to demonstrate that economic and social objectives are intertwined and the implementation the economic objectives might feed-back support and strength to the social objectives, and vice versa.

Directing European economies to new paths of development was the backbone of the Strategy's success. The success could be achieved through increasingly intensive participation of knowledge-based economy in the overall development (research, education, access to information technology) with the concurrent improvement in functioning of a single European market, support for entrepreneurship and strengthening of sound macroeconomic frameworks. The necessary action to accomplish such goals was an intensive enhancement of societies' general knowledge and capability and a constant closing of the social exclusion gap. Special tools were designed to monitor the progress of the Strategy and to provide multilateral support in its implementation.

Since Lisbon, the overall economic performance of the European Union has been modest and some of the ambitions formulated in Lisbon now appear out-of-reach.

This leads to a *second* question: has the Lisbon Strategy provided sufficient impetus to the policy reform agenda in member states and, if not, what else could be done to foster more forceful activism in structural reforms?

With the Lisbon Agenda, EU political leaders made a comprehensive and ambitious commitment. They pledged to make the European Union by 2010 "*the most dynamic and competitive knowledge-based economy in the world capable of sustainable economic growth with more and better jobs and greater social cohesion, and respect for the environment*". This ambitious commitment was further broadened in subsequent European Summits, where leaders undertook to achieve additional

[1] In this paper, the European Union refers to the fifteen member states prevailing when the Lisbon Strategy was adopted, i.e. before the enlargement on 1 May 2004, unless explicitly noted.

objectives in the economic, social and environmental spheres[2]. The European Council eventually adopted a set of 14 quantitative targets that summarize their commitment to economic growth, employment, social, educational, regional and environmental objectives[3]. Of these 14 objectives, five are frequently considered to be particularly important in the economic area: the goal that 70 per cent of those at working age should be employed by 2010, almost 6 percentage points more than prevailing when the Strategy was adopted; the implicit goal that real GDP should grow by 3 percent per year on average[4]; the goal that 50 per cent of older workers should be employed in 2010, compared with 38 per cent at the start of the decade; and the goal that spending on research and development (R&D) be increased from 2 per cent of GDP to 3 per cent by 2010 (Table 1).

Because many of these policy areas are the prerogatives of member states, the Lisbon Strategy is based on the "open method of coordination", a framework which eschews the traditional centralization of policy formulation and relies instead on the peer review of progress made by individual member states. The European Commission regularly monitors the structural indicators targeted under the Strategy[5], and the European Council meets every spring to discuss progress and determine new targets if necessary.

**Table 1. Key EU targets for 2010**

| | 1997 | 2001 | 2010 | European Council |
|---|---|---|---|---|
| Employment rate Total | 60.7 | 64.1 | 70 | Lisbon, March 2000 |
| Age 55-64 | 36.4 | 38.8 | 50 | Stockholm, March 2001 |
| Female | 50.8 | 55 | 60 | Lisbon, March 2000 |
| Effective retirement age | n.a. | 60.3 | Plus 5 | Barcelona, March 2002 |
| R&D as a per cent of GDP Total | 1.86 | 1.98 | 3 | Barcelona, March 2002 |
| Private | 1.1 | 1.2 | 2 | Barcelona, March 2002 |

Source: OECD (2004a)

The first half of the decade has been difficult for the European economy. Output has been moving in fits and starts, without embarking on a sustained expansion. Between 2000 and 2004, annual growth of real GDP was 1.4 per cent on average, less than recorded in the overall OECD (2.1 per cent) and notably less than in the United States (2.5 per cent)[6]. Thus, growth fell short of the goal of 3 percent assumed in the Lisbon Strategy. Admittedly, the overall context was difficult. Just like the early-1980s and early-1990s, the decade started with a cyclical slowdown. In addition, a succession of adverse shocks contributed further weakness, notably the burst of the technology bubble, the scaling-back of business investment, terrorist attacks, corporate scandals and rising oil prices. However, these various influences cannot explain everything. Outside Europe, countries were subject to the same negative influences but, apart from Japan, nonetheless managed to achieve stronger growth. There is therefore a widespread perception that the EU economy is not performing well and risks falling behind other regions.

A more careful examination of the data qualifies this assessment, but does not modify the overall picture. The performance of the United States appears a bit less impressive once expressed in terms of GDP *per capita,* due to the rapid increase of the US population, but it nonetheless remains more robust than that of the EU. This confirms that Europe is not converging towards the level of income prevailing across the Atlantic and has even been diverging from it during the recent period (Chart 1). The widening of the income gap vis-a-vis the United States in the past ten years is a source of discontent for European leaders. It is, therefore, important to understand why the EU is lagging behind.

[2] These various commitments can be found on the web site of the European Commission at the following link: http://europa.eu.int/comm/lisbon_strategy/index_en.html

[3] The 14 basic structural indicators are the following: GDP per capita; labor productivity; aggregate employment rate; employment rate of older workers; education achievement; expenditure on research and development; business investment; comparative price levels; at-risk-poverty rate; long-term unemployment; dispersion of regional employment rates; greenhouse gas emission; energy intensity of the economy; and volume of transport.

[4] The goal of 3 per cent real GDP growth was heavily publicized, but is not officially included in the Summit communiqués.

[5] The most recent statistics related to these structural indicators are provided by the European Commission at the following link: http://europa.eu.int/comm/eurostat/structuralindicators

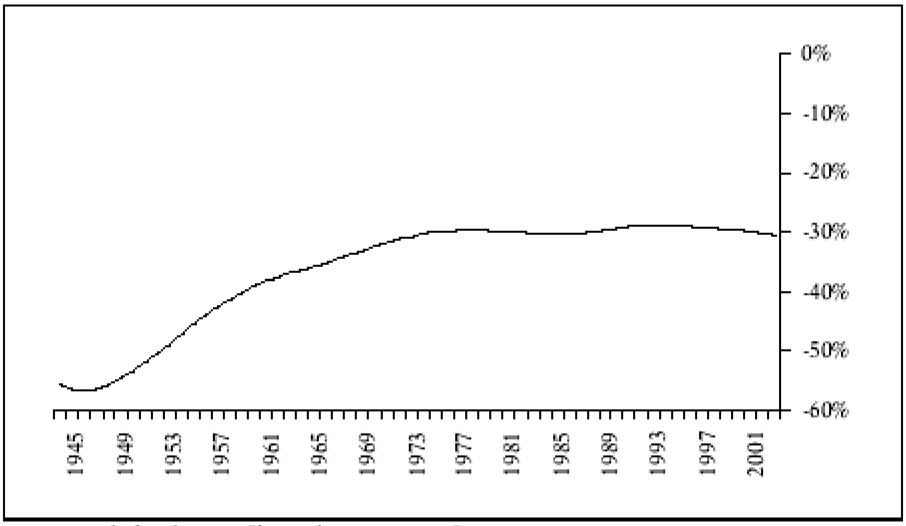
[6] Source: *OECD Economic Outlook* No. 76. Statistical Appendix.

Most analysts use growth-accounting frameworks to assess why Europe is lagging behind. These frameworks, in their simplest forms, decompose *per capita* GDP growth into two components: labor productivity (output per working hour) and labor utilization (total hours worked per person)[7]. Using this approach, the gap between the EU and the US can be decomposed into two components: a gap of 14.4 per cent in labor utilization and a gap of 16 per cent in labor productivity (Table 2). This suggests that the EU needs to achieve stronger performances in both labor market performance and labor productivity, and to remember the goal established through this Strategy.

The reasons for missing the goal of the Strategy should be attributed to the fact that when the Strategy was designed Europe enjoyed very positive development trends, which perhaps led to excessive and unfounded optimism about the future plans and expectations. The origins of such decline were difficult to predict at the early stages of the Lisbon Strategy planning; a general slowdown occurred in economic dynamics and a recession, which followed lasted several years. Does it mean that the important objectives, commonly agreed upon between the countries of Europe in the framework of the Strategy should be abandoned? It seems, however, that frustration resulting from a large discrepancy between hopes and reality hid behind his bitter words.

The official communications of the current Commission strike a significantly different tone as the Commission strives for strengthening and revitalizing of the Lisbon Strategy. The report prepared in November 2004 under the leadership of Wim Kok carries a similar message: he sharply critiques these Strategy's shortcomings, which could have been prevented (for example, too slow introduction of a single market). At the same time, however, Kok emphasizes the importance of the Strategy today in comparison with five years ago: especially now the Strategy should be implemented.

**Chart 1: EU15 per capita GDP gap vis-a-vis the U.S. (2000 PPP, 1945-2004)**




Note: Smoothed with an HP filter with a parameter of 100 over 1921-2011.
Source: OECD, Maddison (2003), EU EPC, U.S. Census Bureau.

**Table 2. Decomposition of per capita GDP, 2002 (United States = 100, PPP exchange rate)**

| | *Per capita* GDP a+b | Effect of labour resource utilisation (a) | Effect of labour productivity (b) |
|---|---|---|---|
| European Union | 71.9 | 85.6 | 84.0 |
| United States | 100 | 100 | 100 |

Source: OECD (2004a)

[7] More precisely, GDP *per capita* is decomposed into three components: labor utilization, labor productivity and the share of working wage persons in total population.

"On the external side, Europe faces the challenge of coping with the acceleration of technological innovation in the United States, illustrated by the market shares gained by U.S. firms in knowledge-related products and services. At the same time, the continent faces the challenge of the economic take-off of China and India and their predominance in labor-intensive markets. European countries also need to address internal challenges, including the financial difficulties of social protection systems and the rapid ageing of its population" (European Commission, 2004; Kok, 2004; OECD, 2004; IMF, 2004; Camdessus, 2004).

We have to agree that the Lisbon Strategy brought limited although very visible results, while its main directions have been rightly chosen and they continue to be valid.

Also, states, which entered the path of competitiveness at a later time, have successfully managed to catch-up. Having this in mind, one could see the future possibilities to implement the Lisbon Strategy more optimistically, under the condition that all countries with due attention and respect treat its goals.

The implementation of the structural reforms proposed by the Strategy is very important also for the new Member States. Going along the Strategy's path they might faster cover the distance separating them from the most developed European countries.

Completing the Single Market, so as to boost product market competition and foster innovation and productivity, seems a good candidate. While the Single Market has promoted competition on goods markets, cross-border competition in the area of services remains impeded by national barriers and various administrative impediments.

The second half of the decade could usefully be devoted to promoting free competition in the field of professional and household services – as foreseen by the EU draft *Services Directive*. By putting this goal at the center of the Lisbon Strategy, the review by political leaders would give Europe a greater chance to become a very competitive and dynamic region by 2010.

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