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Chapter 2

EU AND ECONOMIC GROWTH

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INTRODUCTION

The (then) EU-15 leaders agreed in Lisbon in March 2000 on the ambitious objective to transform the EU by the end of the decade into the "most dynamic and competitive knowledge based economy in the world". The EU leaders envisioned a multi-dimensional strategy aimed at sustainable economic growth (with healthy growth of employment), social cohesion and respect for the environment.

The Lisbon agenda encompasses six broad areas: product markets, capital markets, labor markets, social policies, the environment and 'knowledge' and R&D.

In all these areas, the Lisbon agenda sets lofty goals. Broadly speaking, the EU agenda aims at improving the functioning of the product-, capital- and labor-markets, and simultaneously aims at developing compatible social and environmental policies. Moreover, it specifically targets knowledge and R&D as key to Europe's future economic development.

The Lisbon agenda as such is not really controversial. Improving the functioning of markets and addressing the social and environmental objectives have broad support. However, the agenda is almost all-inclusive, and therefore very difficult to implement. There is just too much in this agenda. Not surprisingly, therefore, the results today -- roughly halfway the 2000-2010 agenda -- are not very encouraging.

Looking at the last five years one can only conclude that Europe has not gained ground; to the contrary, the USA and the Asian economies have outperformed the EU over that period. In a recent assessment, a high-level group appointed by the EU and chaired by the former Dutch prime minister Wim Kok concluded that the member countries have failed to act with sufficient urgency, primarily because of an overloaded agenda, poor coordination and conflicting priorities (Kok, 2004). The Kok-committee formulated two recommendations: i. the Lisbon agenda needs to be prioritized around higher growth and increased employment; and ii. an operational agenda needs to be set-up. That is, according to Kok, the Lisbon agenda misses an operational plan in conjunction with the necessary commitment and sense of ownership by individual member states.

As a caveat, one should realize that a critical assessment of the implementation of the Lisbon strategy is not really surprising. We know that implementing national plans involving structured reforms is difficult, let alone EU-wide action plans. From this perspective, one has to admire the ambitions of the European politicians.

In this paper I will analyze what needs to be done to improve the economic growth in the EU area. I will do this against the backdrop of the political and institutional environment that differentiates Europe from the USA. This also relates to the often heated arguments on American style capitalism vis-à-vis the more gentler and possibly more social European model. An important question here is whether Europe can continue to be different, in particular as it relates to the sustainability of the social welfare state.

I will start out with an assessment of the work by an expert group chaired by Andre Sapir (Sapir, 2003). Sapir provided arguably the most comprehensive analysis of the reforms that the EU might need to accomplish the growth objectives stated in the Lisbon agenda. Following this assessment, I will discuss the institutional focus of the continental European economies as the key distinguishing feature between continental Europe and the USA. I will argue that institutional rigidities are the prime source of difficulty in implementing reform in general, and particularly in Europe. Institutions -- and I really mean institutions in a broad sense: institutions *and* current practices -- adapt slowly, and often are aimed at self-preservation. This indeed, as I will argue, explains in large part the difficulties that Europe has relative to the USA. The USA is less institutionally organized, and is more driven by markets. Not surprisingly, therefore, the American economy is more adaptable than the European one. However, I will develop the argument that this does not *necessarily* mean that the continental European economies *should* lag the USA. Actually, by some measures, for most years after WWII the Europeans economies outperformed the USA, at least up to the nineties. But what will the future bring? Can we expect that Europe will be able to preserve its strong institutional focus? An important issue that I will address is what type of policy measures are needed to augment the competitiveness of the European economies. What type of measures are effective? And what types should governments really abstain from? In doing so, I will address the changes that can be expected in the European economies -- in particular due to the increasing market orientation. My underlying conclusion is that much of the agenda of EU and economic growth is a national agenda. National governments need to revitalize their economies and an effective EU internal market may then help to spur growth.

THE SAPIR REPORT

The work by the Sapir committee (Sapir, 2003) preceded that of the Kok committee (Kok, 2004), but Sapir offered a more comprehensive and far-reaching analysis. The evaluation by Sapir -- compared to Kok -- was equally pessimistic about the possibility of reaching the Lisbon objectives. As in the case of Kok, Sapir's focus was on the measures that would be needed to reach the Lisbon objectives. Indeed, implementation is also in his view crucial, but he went further than that. Sapir emphasized the need for a fundamental reorientation of the EU budget: he argued that the budget as it is allocated today is fully misaligned with the Lisbon objectives. With this view, Sapir tackled politically sensitive issues related to the core functioning of the EU. He also advocated amendments to the stability and growth pact and to the decision making process *within* the EU. Box 1 contains the recommendations from the Sapir report.

BOX 1

POLICIES FOR PROMOTING GROWTH *(FROM "AN AGENDA FOR A GROWING EUROPE", THE SAPIR REPORT, JULY 2003, PAGES 5-6)*

1. *Make the Single Market more dynamic*. Here the main recommendations are for better coordination between regulatory and competition policies to encourage market access for new entrants and to introduce a more pro-active policy to support labor mobility within the Union. A third recommendation is to develop infrastructure to connect up the broader European economy.

2. *Boost investment in knowledge*. The specific recommendations in this context are to increase government and EU spending in research and post-graduate education, to allocate research grants according to the highest scientific standards, to create an independent European Agency for Science and Research, and to encourage private-sector R&D via tax credits.

3. *Improve the macroeconomic policy framework for EMU.* The recommendations here go in the direction of improving the incentives for countries to secure surpluses in good times, while increasing the room for maneuver for fiscal policies in bad times within a framework of strengthened budgetary surveillance and more effective and flexible implementation of the Stability and Growth Pact, while sticking to the 3% ceiling. The Commission should reinforce its surveillance and be given more responsibility to interpret the rules of the SGP. Also, budgetary responsibility would be enhanced by establishing independent Fiscal Auditing Boards in the Member States. At the same time, a higher degree of country differentiation based on the level of public indebtedness should be introduced and the conditions under which the 3% deficit threshold can be breached should be modified. Another set of recommendations concerns policy coordination: there should be greater coordination among national budgeting processes and more dialogue between the president of a newly-established euro area Council, the relevant EU commissioner and the ECB president.

4. *Redesign policies for convergence and restructuring.* In this context, the Report recommends that EU convergence policy should concentrate on low-income countries rather than low-income regions, and that eligibility for access to EU assistance should be reviewed at the end of each programming period. In addition, convergence funds allocated to low-income countries should focus on two areas: (1) institution building, and (2) investment in human and physical capital, leaving beneficiaries free to decide how to allocate resources across different national projects. The Report also recommends EU restructuring support for workers who lose their job and need support to retrain, to relocate or to start a new business, as a complement to national welfare policies. Part of the restructuring efforts should also be devoted to the agricultural sector.

5. *Achieve effectiveness in decision-taking and regulation.* Here the Report makes a series of recommendations: the assignment of competences between the EU and national levels of governance should be more flexibly and coherently defined; the devolution of some funding, economic law enforcement and regulatory functions from the Commission to independent European bodies; further movement towards decentralized implementation of market regulation by developing both steered networks of national and EU bodies operating within the same legal framework and partnerships of autonomous national bodies cooperating with each other and with EU bodies; improvement in the management of the Single Market; strengthening EU methods for implementing the common growth and social cohesion agenda;

institutional reform aimed at strengthening the strategic capabilities of EU institutions, including a leaner Commission (15 members) and more Qualified Majority Voting on economic issues in the Council; and extension of the possibilities for developing more intensive cooperation among subsets of Member States, without defining an a priori threshold for the number of participants.

6. *Refocus the EU budget.* The idea is to reorganize radically that part of the budget for economic actions within the EU. There should be three funds: a growth fund, a convergence fund and a restructuring fund. Eligibility for each kind of spending will be based on separate, but fair and transparent criteria. This restructuring would enable the budget to play a more clearly defined role in achieving the Union's 2010 objectives. If the total budget amount remains unchanged, this will imply a major cut in agricultural spending and the devolution of spending for rural policy to the Member States. Financing the budget should move away from national contributions to sources with a clear EU dimension. Along with changes in expenditures and revenues, the Report recommends changes in budgetary procedures, including the devolution of some responsibility for budget execution to actors other than the Commission.

The analysis and recommendations of the Sapir group make clear that fundamental reform of the EU itself might be needed to make the Lisbon agenda work. Implicitly, the Kok report, by emphasizing the need for national ownership of the agenda, seems sympathetic to this idea. Kok recognizes that the EU by itself is not able to accomplish the Lisbon objectives; a concerted effort of the individual member states is needed. Sapir adds to this that the EU can only play a leading role if it gets its own house in order. In particular, Sapir's recommendations 5. 'effectiveness of decision making' and 6. 'the reallocation of the budget' are aimed at this objective. But also his recommendations 3. 'improve the macro-economic policy framework for EMU' and 4. 'redesign policies of convergence and restructuring', directly address the functioning of the EU, and are ultimately aimed at a more streamlined and effective EU.

It is important to note that both Kok and Sapir underwrite and support the Lisbon agenda. In particular, note the full alignment of Kok and Sapir when it comes to the need to improve and complete the internal market and invest in knowledge and R&D; e.g. see Sapir's first two recommendations: 1. 'make the single market more dynamic', and 2. 'boost investment in knowledge'. Where Kok and Sapir might differ a little is in their assessments of the severity of implementation problems. While both recognize implementation problems, in the case of Kok these are primarily operational, but for Sapir they are more fundamental, and related to core governance issues concerning the functioning of the EU.

AN INSTITUTIONAL PERSPECTIVE

Much of the discussion on the Lisbon agenda is driven by comparisons between the EU and the USA. This is to some extent comparing apples to oranges: the EU is very different from the USA. One key difference between the USA and Europe is that Europe is more institutional, meaning that the societies of Europe are much more organized. For example, in The Netherlands, the corporate sector is strongly organized at the sector and national levels. Labor unions, organizations of employers and the government are in constant consultation with each other in various councils ("institutions"). This leads to all kinds of arrangements that are made mandatory for corporations at large. More specifically, individual corporations are subjected to mandatory wage- and employment agreements agreed upon at the central level. The institutional focus also follows from the perspective of the financial system. Continental Europe is strongly bank-oriented, with a more secondary role for financial markets.

This institutional perspective leads to the conclusion that Europe is more organized than the USA, something that is also apparent from a laws and rules perspective in general; more extensive zoning requirements are just one example. The USA, in contrast, is more market driven, and less organized. What is the impact of this, and how desirable and sustainable are these differences? First, however, let's try to understand the inevitability of institutions both in Europe and the USA. As I will argue, the institutional perspective of the EU in comparison to the USA is a matter of degree, and differences are largely limited to the sector and national levels.

Institutions are a fact of life

The mere fact that we organize economic activities in corporations is already an example of creating institutions. In the "theory of the firm", the core micro-economic subject that analyzes the boundaries of the firm, the creation of firms is typically driven by transaction costs. [1] When market transactions create excessive transaction costs, integrating those transactions (and the parties involved) in a firm might be optimal. Similarly, lack of contractibility may induce opportunistic behavior between parties in the market and could dictate integration and formalized co-operation.

A less well emphasized reason for having institutions is that people often like stability, and to some extent predictability. A corporation (note this is a type of institution) provides such stability, often in the form of job security. This can have distinct benefits. People might be prepared to make firm-specific investments when they expect to stay with the firm for some time. That is, they may choose to invest in skills that are particularly important for the firm they work for, but not (necessarily) for others. The skills then are not marketable, i.e. cannot be used outside the context of the current employer. Without the stability and security that a firm provides, they might not have been prepared to invest in such non-marketable skills. In that case, investing in skills that are marketable would be better from each individual's perspective.

These observations sound abstract, and at first glance their relevance for the debate on the Lisbon agenda and economic growth in general might not be evident. Nevertheless, these observations are of primary importance. The continental European economies are heavily institutionalized. In the case of corporations, job security in Europe is relatively strong, underscoring predictability and stability. Such job security can be interpreted as a hurdle to economic growth: workers my have less of an incentive to work. But it could also have a favorable impact: as stated above, firm-specific investments by workers could be encouraged in this way. The net effect is ambiguous. However, more recently a potentially more important effect has been emphasized. The mere fact of job security may make employers reluctant to hire workers because of the difficulty in laying off workers. Hence job security may backfire, and lead to less employment.

The latter already points at a potential interaction between institutional arrangements (in this case job security) and economic growth (new employment). But there is a more general interaction between economic development and institutional arrangements. An institutionally focused economy typically responds slower to structural changes than a market-oriented economy. Moreover, an institutionally-oriented economy may "smooth"

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[1] See for example Hart (1995).

things (see for example the more balanced income distribution in Europe). This could create rigidities that may undermine economic growth.

Sapir also identified the EU governance structure as an institutional rigidity. In Box 2, I expand on this. However, in this article I will not focus on the rigidities of the EU governmental structure, but rather focus on the rigidities in the European economies versus those in the USA.

Box 2

THE EU IS AN INSTITUTION TOO…

The fifth and sixth recommendations of the Sapir Committee (on respectively the effectiveness of decision making and regulation, and the EU budget) directly address potential rigidities in the EU. Indeed, the EU consists of institutions and practices (some contained in treaties, legislation and regulation) and these could be susceptible to rigidities. The long debates on the new European "constitution" and also the discussions on the distribution of the financial contributions over the member states all potentially point at rigidities in the broad institutional structure of the EU.

Note however that such rigidities can be found in any system of government, also in the USA. What makes the European situation possibly more precarious is that the EU structure is superimposed on national government structures, with considerable, if not most, autonomy preserved at the national level. Such dual structure may well reinforce rigidities.

I discuss next the differences in economic performance of the EU economies vis-à-vis the USA in a historical context.

Slower growth temporary?

The slower response in the institutionally oriented economies of continental Europe has become very apparent during the recent IT revolution. From the mid-1990s on, the European economies have fallen far behind the USA in the dissemination and particularly application of IT. An important question is whether such a slow response implies a permanent lower level of economic performance (and wealth), or whether it just reflects a temporary set-back that will disappear over time. If history could be taken as a guide, Europe will catch up and it will recover the ground it lost to the US. Indeed, looking over the long run, one could conclude that Europe has performed rather well. There have been two periods in history when Europe truly lost ground: the period around 1880, when the sheer unlimited availability of land for agriculture gave the USA a distinct edge, and the period 1914-1950, when wars put Europe at a distinct disadvantage, while the USA was optimally taking advantage of the electricity revolution. Since 1950, Europe has been catching up, and up to the middle of the 1990s, Europe seemed to be closing the gap with the USA. But indeed the picture today is (again) one where Europe is far behind.[2]

[2] See Gordon (2002).

The historical perspective could help explain the current situation. The IT revolution today, and Europe's slow adaptation to this new reality, is reminiscent of the ground that was lost in the period 1914-1950. In that period Europe fell 30 years behind in generic applications of electricity.[3] Only after WWII, Europe started applying electricity in earnest, and managed to close much of the gap.[4] While there were no wars recently, Europe is again behind. Our economic order, and particularly the institutional orientation, might well be the culprit.

From this brief historical overview, one is tempted to conclude that this time, again, Europe will recover its lost ground. A positive interpretation is that the institutionally-oriented model is an alternative to the market-based model, each with advantages and disadvantages. The predictability and security provided by the institutional model may -- as indicated -- have value. And, more importantly, if it only leads to a slower *adjustment* to structural shifts, without permanent effect on (ultimate) welfare, then it might be worth hanging on to. However, the structural shifts now might be much more far-reaching, and it is far from clear that we are only talking about a slower adjustment. It might well be a permanent falling behind. In particular, the shifts that we observe today might threaten the institutionally-oriented model at its core. What I mean is that the IT revolution is much more than a technological shift. The IT revolution fuels and reinforces some other very fundamental shifts in the world order. In particular, the increasingly open borders (globalization) and the ever-increasing competition create profound economic challenges for the institutionally-oriented European economies.[5]

An important question I will address next is whether the institutional focus of Europe can be preserved.

Is the institutional model dying?

The economic order of Europe, and particularly its institutional focus, is to some extent an outcome of social preferences.[6] The greater preference for stability seems universally present. Indeed, where-ever we look -- income distribution, job security, number of prisoners…, etc -- the USA is a country of extremes. Europe has fewer sharp edges. This seems to confirm the desire for predictability and stability. Having said this, the question is whether the European model is sustainable. Clearly, the bad performance over the last few years does not bear well on Europe's chances to preserve its economic order. Indeed, the institutional focus has the inherent risk of rigidity. The challenge is to engage in timely renewal. The institutional perspective seems to protect the status quo. An interesting example is the banking sector. The continental European economies are bank-based, while the USA depends much more on financial markets. Banks are institutions too; their dominance in

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3 In a recent editorial Laura Tyson (2003) rightfully points out that the IT revolution was over-hyped. In particular, the suggestion of a 'new economy' where standard theories of the business cycle would not be at work anymore was plain wrong. But as she correctly emphasizes, the IT revolution will lead to a period of higher productivity growth due to the *application* of IT in the economy at large. This is very much reminiscent of the electricity revolution in the middle of the last century.

4 Total closure of the gap in terms of GDP per capita could not be expected given the differences in preferences for leisure between Europe and the USA, see Prescott (2003).

5 For a rather optimistic, yet nuanced assessment of the prospects of Europe see Svejnar (2004).

6 While it is clearly wrong to talk about *the* European model, the institutional dimension we focus on seems generic to the continental European economies in comparison to the USA. Thus, the institutional focus indeed characterizes continental Europe, but the precise form of the institutional-orientation differs between the continental European economies.

Europe confirms Europe's overall institutional focus. It is interesting to observe that much research has been done on the role of banks in facilitating innovations. Generally, banks are not very good at that. Bank financing seems ill suited for funding new ventures, at least banks do very little of that. In doing so banks very much protect the status quo. Also, the bank-dominated financial systems in Europe allow for little entry into banking, contrary to the USA. This leads to very interesting differences between European and American banking. For example, in the USA mergers between existing banks lead to new entry, while in Europe this is hardly observed.[7]

One of the few generally accepted insights on the adoption of new technologies is that competition, and particularly the threat coming form new entrants, is needed to pressure incumbents into timely adopting new technologies. The European institutional focus often frustrates entry, by protecting the status quo and hence the incumbents. While this was true in the past as well, it seems not sustainable in the future. This type of rigidity has to be dealt with to make the institutionally oriented European economies 'future proof'. Indeed, as hinted at before, the globalization of the world economy, partially inspired by the mobility that information technology creates, makes it increasingly easy to bypass the European economies.

This does not mean that Europe could instantaneously lose its wealth. No, the macro-economic reality is that international trade requires buying and selling. The rest of the world would reap great benefits if Europe manages to keep on buying, for that it needs to have its own economic activity as well. This is not very different from saying that ultimately there needs to be a balance on the current account. Trade theory tells us that countries will specialize based on relative comparative advantages. However, if Europe is not going to slowly retreat in economic importance, it needs to have areas and activities that have some distinct comparative advantage. The general opinion, including that of the composers of the Lisbon agenda and the Sapir and Kok reports, is that that needs to centre around 'knowledge' and a sufficiently adaptable and dynamic internal market. How can this be best accomplished, and is it compatible with the virtues of the European institutional focus?

ACTION PLAN

One of the key lessons of modern research on economic performance is that competition is at the core of increasing productivity.[8] What this means is that the institutional model can only be sustainable if it resolves its inherent rigidities. Indeed, new entrants should not be frustrated by policies that are dictated by incumbents. Many of the legislations and rules in the various countries are effectively entry barriers that are kept in place by the incumbent powers. The financial sector is a nice laboratory. Cruickshank (2000) -- in his evaluation of UK banking -- concluded that existing regulatory practices discourage entry in the banking sector. Since these regulatory practices are (to some extent) shaped by incumbents, it highlights the tendency of incumbents to discourage entry.[9]

7 Interesting research on American data shows that institutions that have grown larger (with or without mergers) are less capable or willing to serve smaller clients, in particular small corporates. This vacuum is filled in the USA via new entry, but this is not observed in Europe. See Rajan and Zingales (2001), Berger et al. (1998) and Boot (2004).

8 For interesting case studies see Chatterjee (2005). See also European Commission (2005).

9 Cruickshank in his evaluation of competition in the UK banking argued that UK regulatory practices impose unjustifiable barriers to entry by effectively requiring that 'new entrants must be linked to an established institution'. Cruickshank also pointed at informal restrictions on who could own a bank,

In general, the political response to threats to the current domestic industrial structure is rather protective. This is understandable. The social costs to economic and structural changes, primarily though temporary adjustment costs, are enormous. However, a protective knee-jerk response is very costly. As the McKinsey Global Institute correctly points out in the context of offshoring jobs: "[Companies] who resist the trend will see increasingly unfavorable cost positions that erode market share and eventually end in job destruction. This is why protective measures to stop companies from offshoring would be a mistake. Offshoring is a powerful way for companies to […] create the jobs for tomorrow".

Obviously, this is a very optimistic characterization of the often painful process of adjusting the domestic European economies to the new realities. Europe, however, has no choice. Its economies need further adjustment, and this process should not be frustrated. However, governments can help this adjustment process particularly by facilitating the generation of new activities. Reducing rules and other rigidities to facilitate entry is one path, and probably the most important. Emphasizing the need for knowledge is another. Indeed, governments do have a role in stimulating R&D and education, cq., knowledge. The real challenge here is to provide for an optimal match between the capabilities of the workforce and the needs of the (future) employers. This requires a multi-facetted approach. Universities play an important role in this but also all kinds of more professional schools.

A particular important element of the agenda should also be encouraging entrepreneurship. The continental Europe economies produce few entrepreneurs. Partially this is related to the elements mentioned (rules and rigidities, lack of training, etc.), in part, however, it is also a cultural problem. Continental European societies at large should become more entrepreneurial and risk taking. This may take time, and one my have to look specifically at new generations. Schools may play a pivotal role in building a more entrepreneurial society.

Governments should be very careful in designing active 'create the winner' economic policies. As an example, let me focus on Silicon Valley in the USA. It is undoubtedly something very nice to have. It is a engine for much economic activity. However, imitating this should not be the objective. Stimulating and facilitating high-tech companies is fine, but it should remain the market sector that makes the choices. More importantly, a blind focus on high tech is missing the point. Growth and employment primarily originate from applications of IT in other industries. This also qualifies the focus on knowledge. Having a highly educated workforce is desirable, but language skills might be more important than high-tech skills.

More active policies are possible, but only if *market conformity* is guaranteed. For example, granting partial public credit guarantees on the financing of small- and medium-sized business could be a sensible policy addressing the frictions that exist in the market for small(er) business credit. Implementation is however key. The experiences in the US and The Netherlands tell that such guarantees are only sensible if the market continues to bear risk as well.[10]

But should governments then be totally passive towards their existing industries? Let me say first that facilitating a good business climate typically also helps existing businesses. Where existing practices are protective of these businesses this may obviously not be the case. However, such protection, as I already indicated, backfires and is not advisable. Going

potentially tougher restrictions on institutions without track record, and higher capital requirements for new entrants. While the FSA (the UK regulator) has forcefully defended its approach to assessing new entrants (FSA, 2000), the Cruickshank report illustrates that the actual practices of regulators and supervisors, and their discretion, could contain the most obvious conflicts with the competitiveness objective.

10 See Boot and Schmeits (2004).

against market forces is just not possible. Again, policies could be thought off that are compatible with the market. As in the case of the partial public sector guarantees, some type of investment related support -- offered in conjunction with the private sector, so shared risk taking -- could be a valuable instrument, and also help existing businesses to adapt and transform.

In the end one has to be very careful about having any illusion that economic development can be planned. The market process, particularly in this period of structural change cannot be predicted. Facilitating should be the rule of the game. And possibly more than just a focus on pure economics is needed. This brings me to the question about the sustainability of the institutional model, and the social cohesion it seeks to build.

Social cohesion is important. It is related to social security but not alone. Let me give the USA as an example. We do not quickly associate the USA with a socially cohesive society. The word social cohesion might also not be the right word, let's call its centrifugal force or just glue. There is are few countries in the world where the people seem so proud to be citizens as in the case of the USA (i.e. to be American citizens). The average American believes in the American dream. This sounds like a cliché, and obviously is a somewhat extreme characterization as well. It is not that rosy, and quite a few people may feel disillusioned. But something like the American dream does exist. Lack of current wealth or (extreme) richness of others is seen as an opportunity. Most Americans seem to believe in their 'model'. Such support or unity is a form of cohesion, but a very different feeling of belonging from that in Europe, but not totally different.

Let me take a very different example. Ireland. This small country, an island actually, is the economic miracle of the last 20 years. Hard facts, like its accession to the EU with its large benefits in terms of inflow of EU structural funds, the tax competition it chose to engage in to attract international businesses, the stable political climate, and sensible economic policies, all help explain its success. But one important factor is missing in this list. Indeed, its social cohesion. This is and was enormous and allowed for a very coherent and coordinated expansion. Together with pure luck and reinforcing opportunities, Ireland became a success story.

What I try to tell with the USA and Irish examples is that economic growth does require a feeling of unity, and this feeling can take very different forms. This has implications for the institutional focus of the continental European countries. This is in part motivated by cohesion, and thus something to preserve. It is important to have such social cohesion not translate in exclusion for non-incumbents. The real challenge for the institutional model is to be all inclusive and thus adapt to newcomers and new realities. [11]

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[11] I did not address the sustainability of the social welfare state directly. The discussions in the Scandinavian countries and The Netherlands are about redefining the social welfare state. Rather than just *supporting* the weak, the language is shifting in the direction of *investing* in people and making them stronger and better able to take care of themselves such that they can take advantage of opportunities.

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