Arenas ekonomiska råd

Rapport 6

Arenagruppens Economic Council 2012, 25th October, Stockholm

The Industrial High Road to Sustainability and Growth

FRIEDRICH EBERT STIFTUNG

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Introduction

On October 25, 2012 Arenas Economic Council and Friedrich Ebert Stiftung conducted its annual international economic conference. The theme and discussions 2012 established the links with the European economic crisis. But the focus was mainly on finding strategies to formulate a modern industrial policy that can create new jobs, full employment and a social and environmentally sustainable economic development.

In this report, we have collected several of the presentations at the seminar. An introductory text summarizes the presentations and discussions. Some of PDF presentations are attached at the end of the document.

These discussions will continue because it concerns Europe's future economic development. And the possibility of developing a social European model which is now seriously threatened.

Håkan A Bengtsson
Arena Group CEO

Gero Maaß
Director of the Friedrich Ebert Stiftung's Nordic Office

Third Annual Conference of
Arena's Economic Council

THE INDUSTRIAL HIGH ROAD TO SUSTAINABILITY AND GROWTH

Stockholm, 25th October 2012

Conference Program

Background and aim

The escalation of the crisis in Europe poses the greatest threat to global prosperity today. To find a way out of this vicious cycle one needs a comprehensive investment and growth program. From a progressive perspective such a program needs to develop a stronger focus on the real economy, the modernization of structures, improved competitiveness, increase of value added, substantially raising the level of sustainability and eventually the strengthening of European integration. In the current debate, however, competitiveness is often interpreted in a rather narrow economic understanding with an asymmetric focus on the level of taxation, the nature of labour or environmental legislation as well as qualitative assessments of access to finance, etc. Today, after the debt-fuelled growth model has failed spectacularly and was on top of that mistaken as a symbol of competitiveness, only marginal intellectual departures from the concept have taken place in major parts of the political discourse.

Together with global experts and decision makers we aim to discuss a sophisticated progression of competitiveness, identify key drivers of sustainable competitiveness and industrial policies in various countries as well as within the European and global institutional settings.

Guiding Questions

(1) What are the progressive concepts to increase innovation and develop more comprehensive concepts of competitiveness embedded into the European framework as well as demands from globalization?
(2) What is a progressive understanding of an industrial renewal against the background of concepts of ecological industrial policies?
(3) Which instruments and policies can be identified in order to strengthen our countries' economy as a whole? Which macroeconomic framework is needed in order to support these instruments?

The organizing institutions are the Friedrich Ebert Foundation and the Arena Group in Stockholm:

Arena Group is one of the premier progressive think tanks in Scandinavia. The Arena Group's Economic Council is an initiative with the aim of providing space for progressive economic thinking and stimulating independent economic research. The council attracts researchers from a broad range of academic disciplines, journalists as well as an interested public.

Friedrich Ebert Foundation is an independent NGO, associated with the German labor movement. With offices and activities in more than 100 countries, FES is dedicated to promoting the values of social democracy.

Registration
If you want to attend our conference, please sign up here: fesnord@fesnord.se

Time
10.00 – 15.30, Thursday, 25th October 2012

Venue
LO, Barnhusgatan 18, Stockholm

Organizers
Gero Maaß, Director Nordic Office, Friedrich Ebert Foundation, Stockholm
E-mail: gero.maass@fes.de
Tel: +46-8-454-65-92

Håkan A. Bengtsson, CEO Arenagruppen
E-mail: hakan.bengtsson@arenagruppen.se
Tel: +46-7-06646236

25th October 2012

10:00 **Opening Address**
Håkan A. Bengtsson (Arenagruppen)
& Karl-Petter Thorwaldsson, LO Chairman

10:15 **Panel 1: Comparing Models of Comprehensive Competitiveness – The Analytical Perspective [20 min input each]**

"Why Rich Countries got Rich …"
Erik S. Reinert, Tallinn University of Technology and Gunnar Myrdal Prize Winner

"What will be the US way to go?"
Jennifer Erickson, Director of Competitiveness and Economic Growth at the Center for American Progress

"How Germany attempts to builds a New High Road …"
Daniel Buhr, expert for Policy Analysis and Political Economy, University of Tübingen

11:15 **Coffee Break**

"When a country deviates from the High Road
– what can be learnt from the case of Denmark?"
Bengt- Åke Lundvall, Innovation expert at Aalborg University

"Innovation Policy for Growth and Sustainability
– Some Swedish experiences and the way forward"
Charles Edquist, expert for innovation processes, innovation systems and innovation policy at Lund University

12:00 **Discussion with the Panel and the Audience**
Moderator: **Jesper Bengtsson,** Journalist

12:45 **Lunch Break (Sandwiches)**

Arenagruppen's Economic Council 2012, 25th October, Stockholm
The Industrial High Road to Sustainability and Growth

Opening Address

Håkan A. Bengtsson
Håkan A. Bengtsson is founding member and former chief editor of Arena. He is author and editor of several books and articles about Swedish politics. Today he is Director of Arena-gruppen.

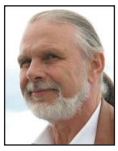
Karl-Petter Thorwaldsson
Karl-Petter Thorwaldsson is chairman of LO, the Swedish Trade Union Confederation since 2012. Before, he was Ombudsman for international questions and collective agreements at the trade union IF Metal.

Panel 1: Comparing Models of Comprehensive Competitiveness – The Analytical Perspective

Erik S. Reinert
Erik S. Reinert is professor of Technology Governance and Development Strategies at Tallinn University of Technology. Reinert's research interests and publications focus around the theory of uneven development and the history of economic thought and policy. With his book "How Rich Countries Got Rich ... and Why Poor Countries Stay Poor", he won the Myrdal Prize in economics.

Jennifer Erickson
Jennifer Erickson is the Director of Competitiveness and Economic Growth at the Center for American Progress (CAP). Her work focuses on a range of issues affecting America's ability to compete successfully at home and internationally. Prior to joining CAP, Jennifer served as special adviser to the First Minister of Scotland, with portfolios including economic growth, innovation, and U.S. relations.

Daniel Buhr
Daniel Buhr is Professor for Policy Analysis and Political Economy at Tübingen University since October 2010. His research is organized around governmental coordination of innovation policy in the state and justice in the welfare states.



Bengt-Åke Lundvall
Bengt-Åke Lundvall is professor of economics at the Department of Business Studies at Aalborg University, Denmark. His research focuses on public policy and theoretical issues related to innovation systems and learning economies. He developed the idea of 'the learning economy' in collaboration with Björn Johnson. From 2004 to 2006 Bengt-Åke was Deputy Director of the OECD Directorate for Science, Technology and Industry.

Charles Edquist
Charles Edquist holds of the Ruben Rausing Chair in Innovation Research at Lund University. He is member of the Research Policy Advisory Committee to the Swedish Government. Charles is a founding member of CIRCLE (Centre for Innovation, Research and Competence in the Learning Economy) at Lund University.

Panel 2: Progressive Policies Required – The Political Perspective

Stefan Löfven
Since January 2012 Stefan is Chairman of the Social Democratic Party of Sweden. Before, he was leader of the trade union IF Metall for more than six years. In September 2012 he presented the so-called "Business-plan" of the social democrats. This strategy-paper proposes heavy investment in Education and R&D in order to foster Sweden's international competitiveness and triggered a national debate.

Michael Vassiliadis
Michael Vassiliadis is Chairmen of the German Mining, Chemical and Energy Industrial Union (IG BCE). He is President of the European trade union IndustriAll since 2012. Furthermore, Michael is member of the Parliamentary Advisory Council on Sustainable Development.

Nick Pearce
Nick Pearce is Director of the Institute for Public Policy Research (IPPR), having rejoined the institute in 2010 after serving as Head of the Policy Unit at the British Prime Minister's Office. Nick is an author and regular commentator on public policy in broadcast and print media.

Closing Remarks

Gero Maaß
Gero Maaß is Director of the Nordic Office of the Friedrich-Ebert-Stiftung, Stockholm. Before, he was head of the International Policy Analysis Unit of the Friedrich-Ebert-Stiftung, based in Berlin and Director of the FES offices in London and Paris.

The panel discussions will be moderated by:

Jesper Bengtsson
Jesper is chief editor of the magazin OmVärlden and works as editorialist for the Swedish Daily Aftonbladet.

Arenagruppen's Economic Council 2012, 25th October, Stockholm
The Industrial High Road to Sustainability and Growth

The Industrial High Road to Sustainability and Growth

The escalation of the crisis in Europe poses the greatest threat to global prosperity today. To find a way out of this vicious cycle one needs a comprehensive investment and growth program that puts European economies on a new level.

After the debt-fuelled growth model has failed spectacularly, we have to reconsider the concepts of competition and sustainable economic growth: In order to make a lasting investment, a progressive growth program has to focus on the real economy, the modernization of structures and eventually the strengthening of European integration.

The current debate, however, is overshadowed by a rather asymmetric conception of competitiveness focusing on the level of taxation, the nature of labor or environmental legislation as well as qualitative assessments of access to finance.

The Economic Council Conference 2012, organized by the Nordic Office of the Friedrich Ebert Foundation and the Swedish Think Tank Arena Gruppen, brought together international experts and decision makers in order to discuss the following questions:

- What is a progressive understanding of industrial renewal and how could a sophisticated progression of competitiveness look like?
- What macroeconomic framework is needed in order to support these instruments?
- What instruments and policies can be identified in order to strengthen the sustainability of the EU's economy as a whole?

Competition – A two-sided Concept

Before delving deeper into the question how innovation policy can help to overcome Europe's current crisis, we have to clarify the relevant concepts: What exactly is innovation and how is it related to competitiveness? What makes an economy grow and how do we evaluate the sustainability of economic growth is sustainable?

According to Erik Reinert, competition is a somewhat two-sided concept: One the one hand competition can be defined as the ability of a nation to sell its products in international markets at rising levels of national wages. On the other hand, however, it can be defined just the other way around: In this case innovation is development that leads to lower wages in order to have a competitive advantage over other countries.

A classic example worth mentioning in this context is the invention of the spinning jenny in the 18th century. It illustrates that innovation has to be seen as a process: Initially, the creation of a high-quality product triggers technological or even social progress, e.g. the invention of a machine that facilitates the production of a certain good, for example yarn. This phase is characterized by investments in R&D which allows optimizing production methods, increasing returns and rapid technological progress. It may even trigger synergy effects leading to innovation in other sectors. Thus, innovation constitutes a source of Economic growth.

In this stage a skilled and well paid workforce is required to develop and operate new machinery which results in a high market value of the good. At the same time it creates jobs and thus enhances the middle class.

After a certain period the former high-quality product becomes a cheap mass product with a low market value. As it is based on old knowledge, other competitors are able to copy the good and further reduce prices. Moreover, process innovations lower the demand for skilled labor. As a result wages and the number of workers are decreasing. In the end, the formerly innovative good does not any longer have the positive economic impact it had at its birth.

The pressure to produce at lower costs adds a geographical element to the two-sided concept of competitiveness and constitutes a central challenge modern economies are faced with: The outsourcing of production to low-wage countries.

Productive and unproductive capital

Besides the process of innovation itself, Erik Reinert argues that capital markets play a vital role and have to be included in the analysis.

Capital lays at the very basis of innovation. It virtually is the lube oil of the innovation process, which transforms a good idea into a working machine.

According to Reinert's interpretation, the current European financial crisis poses a threat to innovation and competitiveness. He refers to a more general phenomenon that hinders innovation, "conspicuous consumption". This term has been developed by the US-Norwegian economist Thorstein Bunde Veblen (1857-1929) and describes the negative impact of unproductive capital, which does not contribute to economic and social progress. This is for instance the case when money is invested in prestigious but unproductive luxury goods.

The role of financial Markets

According to Reinert, today's financial markets are flooded with "conspicuous products" which allow making money "through predatory activities". Rather than providing capital that 'oils' the process of innovation, financial markets offer speculative products that even hinder innovation. "We have to understand that most of the serious money which is being made is made in ways which do not contribute to innovation and increasing living standards", Reinert argues.

To support this argument, Reinert refers to the Italian economist Pietro Verri, who stated that "the private interest of each individual is the safest guarantor of public happiness only when it coincides with the public interests". Reinert identifies the unregulated financial markets as the underlying problem of the current crisis because it attracts 'unproductive' capital which is lacking as investments in the 'real' economy. The need to channel capital towards efficient investments that enable economic and social progress is a theme politics has to deals with: "We have to invest, in order to put our economies on new industrial level", Reinert argues.

Innovation policy is "midwife" of sustainable economic growth!

Having introduced the concepts of competition and innovation from a historical perspective this section will take a closer look at the way politics should deal with innovation. Charles Edquist is one of Sweden's leading researchers in this field. On the Economic Council Conference 2012 he defined innovation policy as "all actions by public organizations that influence innovation processes." Consequently, innovation policy unintentionally interferes with various other policy areas.

Edquist describes innovation as a phenomenon that does not occur "inside closed units". Instead it is a social process that is created when people interact and approach a problem from different perspectives. Innovation is an indefinite process that often stretches over decades, and reaches different stages, as described before. Sometimes innovation is a diffuse, intangible development, yet, it provides crucial economic and societal dynamic. Therefore, it deserves special political attention and coordination e.g. by an Innovation Policy Council as it is the case in Sweden (chaired by the Swedish Prime Minister).

According to Edquist, it is also important to bear in mind that innovations are tangible (e.g. infrastructure) but also intangible (social learning) and do not only take occur the private but also in the public sector. Edquist claims that innovation is a unique policy filed that is "superior" to other ones as it pursues a holistic approach that comprises a wide range of activities. This of course includes activities that are closely linked to certain industries, however, the terms industrial- and innovation policy should not be used interchangeably. Edquist identifies a crucial difference between these two subjects: While the first is future-oriented, the latter is burdened by support to "old and dying sectors" (which reached the end of the innovation process).

From Edquists perspective this distinctive difference is a major obstacle for sustainable economic growth: politically, it often seems more convenient to support old industries in order to save jobs – and eventually votes. However, Edquist argues that in most cases such a policy is not successful in the long run. On the contrary: Policy should support sectors that "do not have a lobby", in order to prevent investments in outdated technologies.

Metaphorically speaking, Edquist compares innovation policy with the job of a "midwife": it provides care for young technologies and helps them growing up. When they are mature, they have to care for themselves. Normally, market economy provides incentives to create innovation. However, under certain circumstances public actors should intervene, for example when additional funding and coordination is needed to facilitate strategic and extensive research or marketing.

Finally, Edquist presented the so called Swedish paradox to illustrate the need for state intervention. Despite high R&D spending in Sweden, returns are comparably low. To overcome this problem the Swedish government introduced the public procurement for innovation policy (PPI), which obliges the government, to spent 10 % of annual public procurement on innovations that potentially contribute to sustainable economic growth.

300 million engines of growth: Why the US has to rediscover middle class policy

Having discussed innovation policy from a top-down perspective (the role of public institutions), this section will approach the subject from a bottom-up perspective. According to Jennifer Erickson the role of consumers is a crucial factor that determines the environment for innovation: Only if new products meet the demand of the market, a good idea will make an impact. In her presentation Erickson illustrates that the economic well-being of the US middle class has been neglected by politicians for too long. She argues that purchasing power of a broad middle class is a decisive factor of economic growth and innovation.

According to Erickson, the last three decades were characterized by an imbalanced distribution of US income: the median family income only rose by 35%, while the income of the wealthiest 1% of society rose by almost 280%. Actually, this development was politically wanted, as US politics followed the idea of supply-side or "trickle-down" economics. This theory assumes that economic growth is unleashed primarily by the investment activities of the wealthy – which should therefore be incentivized by low taxes and minimal regulation.

Yet, this policy led to dramatic social inequality. Erickson pointed out that the top 1% percent enjoyed an annual income growth of more than 90% while the general population only gained an annual plus of 7% in 2009. Today, the economic crisis even decreases the income of median U.S. households to the level of 1995. Erickson argues that such an income distribution is not only a normative question of social justice. In fact it also disturbs the overall economic development of the U.S. According to Erickson, "trickle-down" economics since the late 1970s led to "a nearly four-decade track record of failure" resulting in today's severe economic situation.

The underlying problem of a weak middle class lies within the marginal propensity to consume, which is much higher for lower and medium incomes than for high one. In other words, high earners save more of their income (to spend it on "conspicuous goods"), while a strong middle class creates a stable source of demand for goods and services. Moreover, a strong middle class that demands good governance, property rights, infrastructure and education lays the foundations for a stable economic environment that facilitates innovation. Good education and training enables people to start a business and finally guarantees "economic mobility", the chance to do economically better than one's parents.

As Jennifer Erickson pointed out in her presentation there are good reasons to include the theme of a strong middle class and social justice in the discussion about sustainable economic growth. In face of growing economic and social disparities within the EU, which are tightened by the current paradigm of austerity, the American situation should also be taken into account in Europe.

Germany between the low and high-road: Did "Social Growth" drop by the wayside?

Germany has shown a remarkable economic dynamic during the past decade. The reasons for this development certainly lay in major reform projects, such as "Agenda 2012" and the "Hartz" policies, promoted by the coalition government of Social Democrats (SPD) and the Green Party. This set of labor market and social insurance reforms certainly enhanced the German labor market and the country's international competitiveness. However, these policies are still contested - also within the SPD and trade unions which openly opposed the largest cut into the social security system since World War II. Moreover, statistics

show that an increasing number of temporary jobs and a growing low wages sector without sufficient social insurance coverage. Thus, there are reasons to question the sustainability of Germany's recent economic development.

Referring to Reinert's definition of competition, these measures reflect the negative dimension of competitiveness. Consequently, Buhr argues that the "Agenda 2010" and "Hartz" policies first and foremost contributed to a "low-road" of economic growth. The positive economic dynamic of the recent years was mainly due to labor-market and social policy reforms, which constitute a trend "of problematic growth". Especially the service sector is driven by low wages and short term jobs – a development that has diffuse externalities, which might become a burden for the future.

At the same time, Buhr's analysis shows that Germany set the course for a more sustainable development: Investments in renewable energy ("Energiewende") going along with an intelligent restructuring of the energy supply system are certainly part of a "high-road" policy. Additionally, the Government has set ambitious goals for the mobility sector and envisages one million electric vehicles in Germany by 2020. This focus is partly in line with the idea of the "Third Industrial Revolution", a term developed by the US American economist Jeremy Rifkin. He demands heavy investments in new, environmentally friendly and sustainable technologies which will dramatically increase productivity and set whole economies on a new level. Yet, financing models that provide sufficient funds for such a move are still to be developed.

Generally, the federal R&D budget rose from 9,0 billion in 2005 to 12,8 billion in 2011. However, the expenditures for R&D in Germany's federal states are highly heterogeneous: While Baden-Wurttemberg invests 4,79% of the regional GDP the rural state of Schleswig-Holstein only uses 1,25% for R&D. Thus, it remains to be seen how governments could provide initial funding for radical infrastructural reforms let alone question how they will politically justify a policy that probably demands new debts.

Besides the abovementioned investments in new infrastructure that triggers sustainable economic growth, Buhr highlights another concept that should be considered in this context: "Social growth". Although unemployment in Germany is currently at a record low, Buhr claims that the recent years were characterized by growing social inequality. Also a coordinated market economy such as Germany is affected by the trend of a shrinking middle class that is to some degree comparable to development the U.S. but less significant. As a result, decreasing incomes coupled with growing number of temporary jobs limits domestic demand and exports of other EU countries at the same time. The low demand of Europe's largest economy in fact has a negative impact on the current crisis in other member states.

"Industrial growth needs an active state that prepares the seedbed for innovation!"

Similarly to Germany, Sweden is performing relatively well during the current European crisis. Yet, Stefan Löfven, leader of the Swedish Social Democratic Worker's Party, observes a negative economic trend, which significantly lowers Swedish competiveness. Löfven points out that the last few months have been dominated by reports about research based companies such as AstraZeneca and Sony Mobile leaving for other countries. Generally, he blames the right wing government to have succeeded in increasing inequality, but not lowering unemployment or creating new incentives for growth. According to Löfven, Sweden is generally suffering from insufficient structures for innovation and lacks research diversity. As research is focused on a few key companies, Sweden is vulnerable for companies downsizing or moving abroad.

Furthermore, especially small and medium-sized enterprises, lack capital to secure business expansions. Another problem are spending cuts in the education system which led to a growing gap between the general education level of the workforce and the demands of growing companies. Most importantly, Löfven argues that Sweden lacks an efficient cooperation between society, academia, companies and trade unions. In contrast to the government, he sees a leading role of the state in this field: "Companies ask for more support from the government and more forums for cooperation and coordination", Löfven reports. Good policies can be a "seedbed for innovation and industrial growth", says Löfven.

He argues that the state should take a leading role because it has the capability to oversee the whole process chain of innovation that links the various parts of a society. Accordingly, he demands investments in public research: "Education is at the core of Social Democracy as it reinforces both equality and the

economy at the same time!" A well educated workforce and measures of lifelong learning are the very basis of sustainable growth because it increases the flexibility of a society and allows to adapt quickly to new economic situations. By increasing access to research, capital and a skilled workforce Löfven wants to strengthen "all the key parts along the innovation chain".

"We have to cure the British disease!" – How asset bubbles hinder sustainable growth

The banking and financial services sectors of the City of London dominate the United Kingdom's economy. In contrast to other European economies, these sectors make up a significant share of the countries' GDP. In his contribution, Nick Pearce, Director of the Institute for Public Policy Research based in London, provides an insight into the economic situation of a country that has been tremendously affected by the financial crisis. In fact, the 2008–2009 recession was the longest since records began.

According to Pearce, Britain's economy remains very instable even today, after the most critical phase of the crisis seems to be over. The country still has the highest private household debt in G7. Statistics show that household debt relative to income is still higher in the UK than in the US and the eurozone. In contrast to previous speakers before, Pearce focused on the contemporary problems linked to the unique role of the financial sector of his country.

In order to tackle the countries vulnerability, a central political task will be the restructuring and regulation of the financial sector. The narrowness and weakness of the tax base has to be tackled, as well as speculation in the City of London: "We have to cure the British disease", which produced one asset bubble after another, says Pearce. Private consumers but also banks have to stop lending each other money that does not exist. To this end, Pearce stipulates a consolidation of "too big to fail" banks and legal measures against highly speculative businesses – a claim that is in line with Reinert's conception of "conspicuous goods".

As the economically important but currently crisis-ridden financial sector contributes only little to public budgets, the government's room to set new economic incentives is limited. Due to the weak fiscal situation in the UK, Pearce forecasts difficult spending choices. Additionally, the government is lacking a clear strategy to channel investments in new technologies, as Daniel Buhr has demonstrated for the German case. Certainly, the UK has a capable research system. However, similar to Sweden, Pearce sees a problem when it comes to coordination between private economy and relevant institutions that are linked to the process of innovation, e.g. the education system.

Long term planning instead of short-lived success increases trust in innovation

"Do we want to follow a high road strategy?" That is how Hilmar Höhn, Head of the Liaison Office Berlin of the German industrial trade Union IGBCE, opened his talk at this year's Economic Council Conference. From his perspective, a major problem of industrial and innovation policy is the fact that "people have lost trust in economic progress and innovation with the exception of the iPad or iPhone". What is the reason for this pessimistic assessment?

The answer to this question is related to the way economic growth is created and distributed within an economy. The German "Energiewende", the transition to renewable energy, has been mentioned as a positive example for sustainable growth before. Höhn, however, sees this policy more critically: "There is a general consensus about the goals, but actually, we have no idea how to reach them". In fact, rising costs for energy put a heavy burden on consumers. "If innovation is associated these negative aspects, citizens will take an increasingly critical stance on economic renewal", he argues. Instead, innovation and economic growth have to make a positive social impact on the people. This can only happen if it strengthens the real economy.

According to Höhn, the following conditions have to be fulfilled to meet this requirement: First, the economy as a whole has to rediscover the importance of long term planning instead of short-lived success and maximized profits. Investors and markets have to give time, so ideas can grow. Economic growth has to be based on real values and not on fictitious assets.

Secondly, politics and public administrations have to follow long-term strategies, too. This includes

investments in education systems and a qualified workforce building the foundation of any innovative and productive economy. Likewise, financial resources have to be made available for companies that are willing and able to engage in research. Again, like other speakers have stressed before, a close cooperation between industries and academic institutions is a necessity.

Thirdly, the networked nature of Europe's economies has to be taken into account: Production and consumption do not stop at national borders; therefore Europe's entire value added chain has to be modernized.

Panel 1:
Comparing Models of Comprehensive Competitiveness
– The Analytical Perspective

Erik S. Reinert

Erik S. Reinert is Professor of Technology Governance and Development Strategies at Tallinn University of Technology. Reinert's research interests and publications focus on the theory of uneven development and the history of economic thought and policy. With his book "How Rich Countries Got Rich ... and Why Poor Countries Stay Poor", he won the Myrdal Prize in economics.

Charles Edquist

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Jennifer Erickson

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Daniel Buhr

Daniel Buhr is Professor for Policy Analysis and Political Economy at Tübingen University since October 2010. His research is organized around governmental coordination of innovation policy in the state and justice in the welfare states.

Panel 2:
Progressive Policies Required
– The Political Perspective

Stefan Löfven

Since January 2012 Stefan is Chairman of the Social Democratic Party of Sweden. Before, he was leader of the trade union IF Metall for more than six years. In September 2012 he presented the so-called "Business-plan" of the social democrats. This strategy-paper proposes heavy investment in Education and R&D in order to foster Sweden's international competitiveness and triggered a national debate.

Nick Pearce

Nick Pearce is the Director of the Institute for Public Policy Research (IPPR), having rejoined the institute in 2010 after serving as Head of the Policy Unit at the British Prime Minister's Office. Nick is author and a regular commentator on public policy in broadcast and print media.

Hilmar Höhn

Hilmar Höhn is Head of the Berlin Liaison Office of the German Mining, Chemical and Energy Industrial Union (IG BCE).

5. Eric S Reinfert:
Why rich countries got rich – and why they sometimes lose their wealth

Why rich countries got rich – and why they sometimes lose their wealth

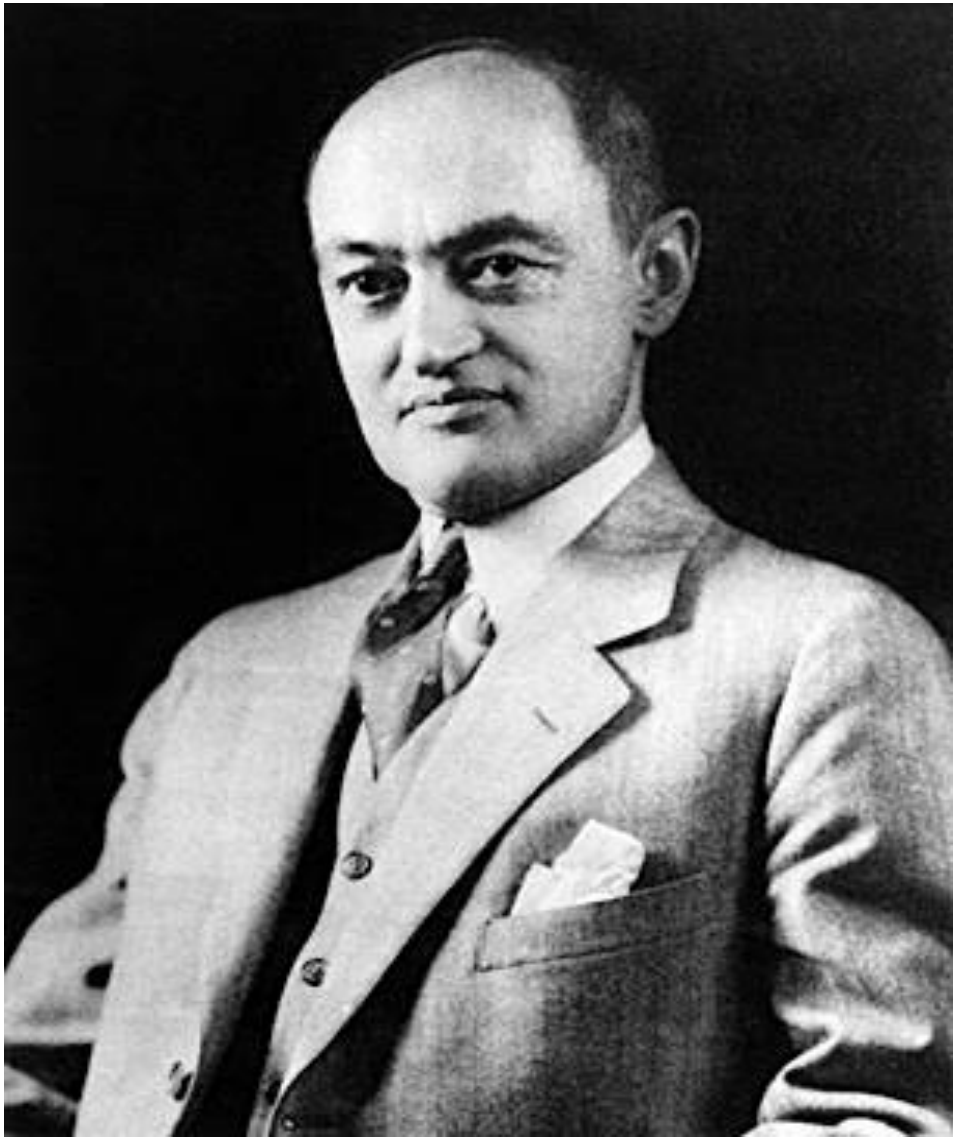
Erik S. Reinert

Res Publica, Oslo & Tallinn University of Technology, Estonia.

«Competitiveness»

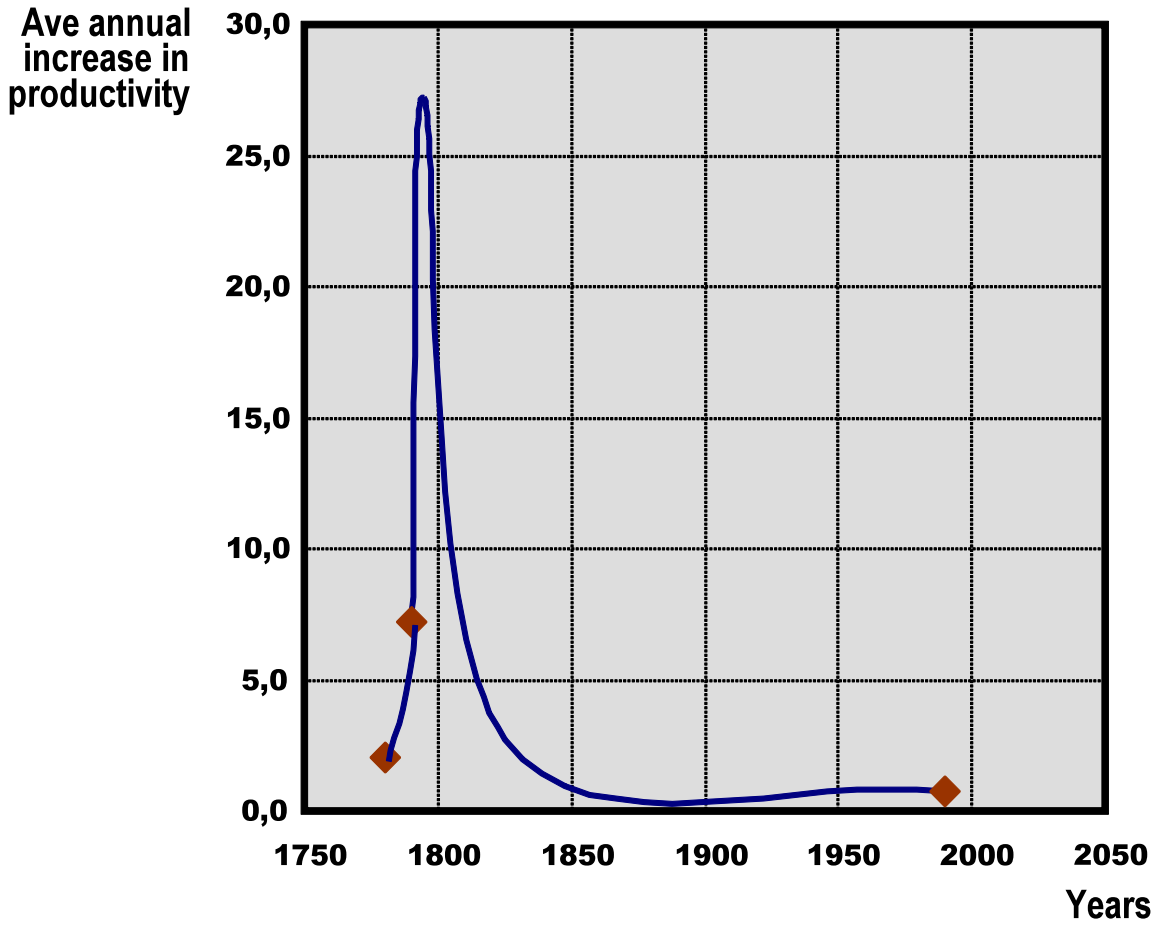
Definition 1. Ability of a nation to sell its products in international markets at rising levels of national wages.

Definition 2. A country's advantage or disadvantage in selling its products in international markets (meaning that in order to be competitive you may have to lower wages)



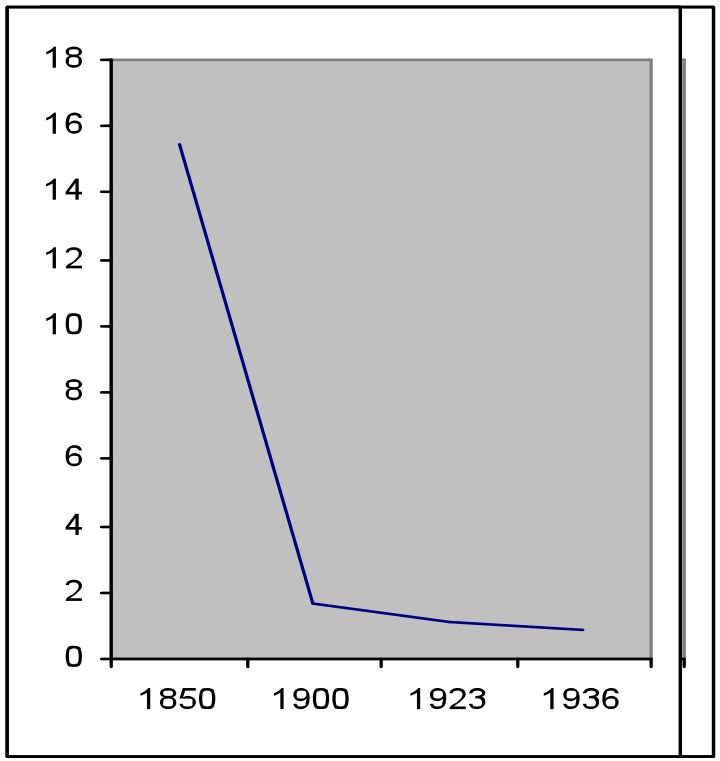
Joseph Schumpeter (1883-1950)

Activity-specific Economic Development:
The mechanization of cotton spinning during the First Industrial Revolution.



Source: Carlota Perez, Calculations from Jenkins 1994

USA: Learning Curve of Best-Practice Productivity in Medium Grade Men's Shoes'.



Man-Hours Required by Best-Practice Methods of Producing A Pair of Medium-grade Men's Shoes at Selected Dates in the U.S.

Year	Man-Hours Per Pair
1850	15.5
1900	1.7
1923	1.1
1936	0.9

ECONOMIC ACTIVITIES ARE QUALITATIVELY DIFFERENT!
Choose GOOD (Schumpeterian), not BAD (Malthusian) Activities

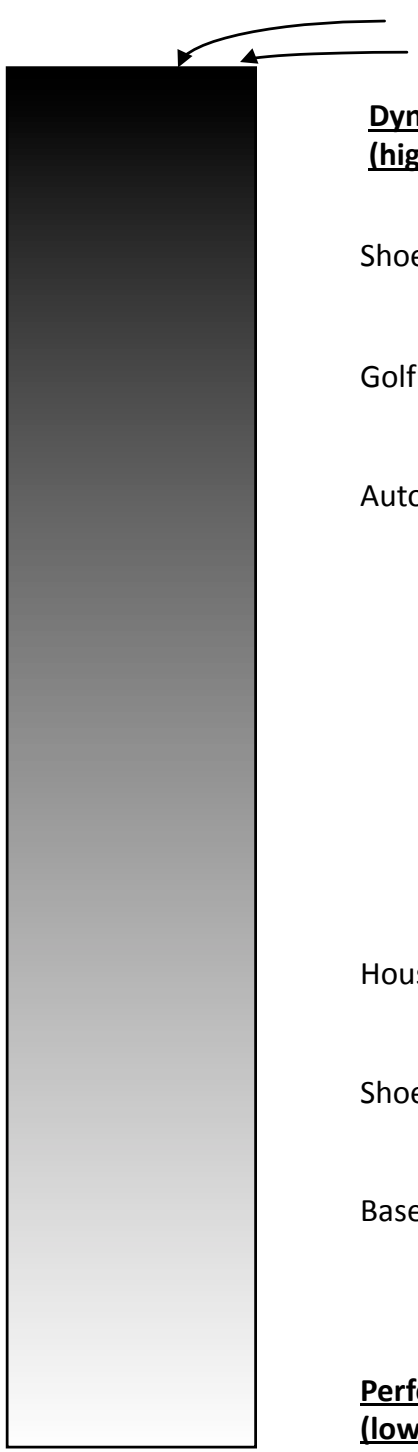
‘Good’ export activities

- Increasing returns
- Dynamic imperfect competition
- Stable prices
- Generally skilled labour
- Creates a middle class
- Irreversible wages (‘stickiness’ of wages)
- Technical change creates higher wages to the producers
- Creates large synergies (linkages, clusters)

‘Bad’ export activities
if no Schumpeterian sector present

- Diminishing returns
- ‘Perfect competition’ (commodity competition)
- Extreme price fluctuations
- Generally unskilled labour
- Creates ‘feudalist’ class structure
- Reversible wages
- Technical change tends to lower prices to the consumers
- Creates few synergies

The Quality Index of Economic Activities

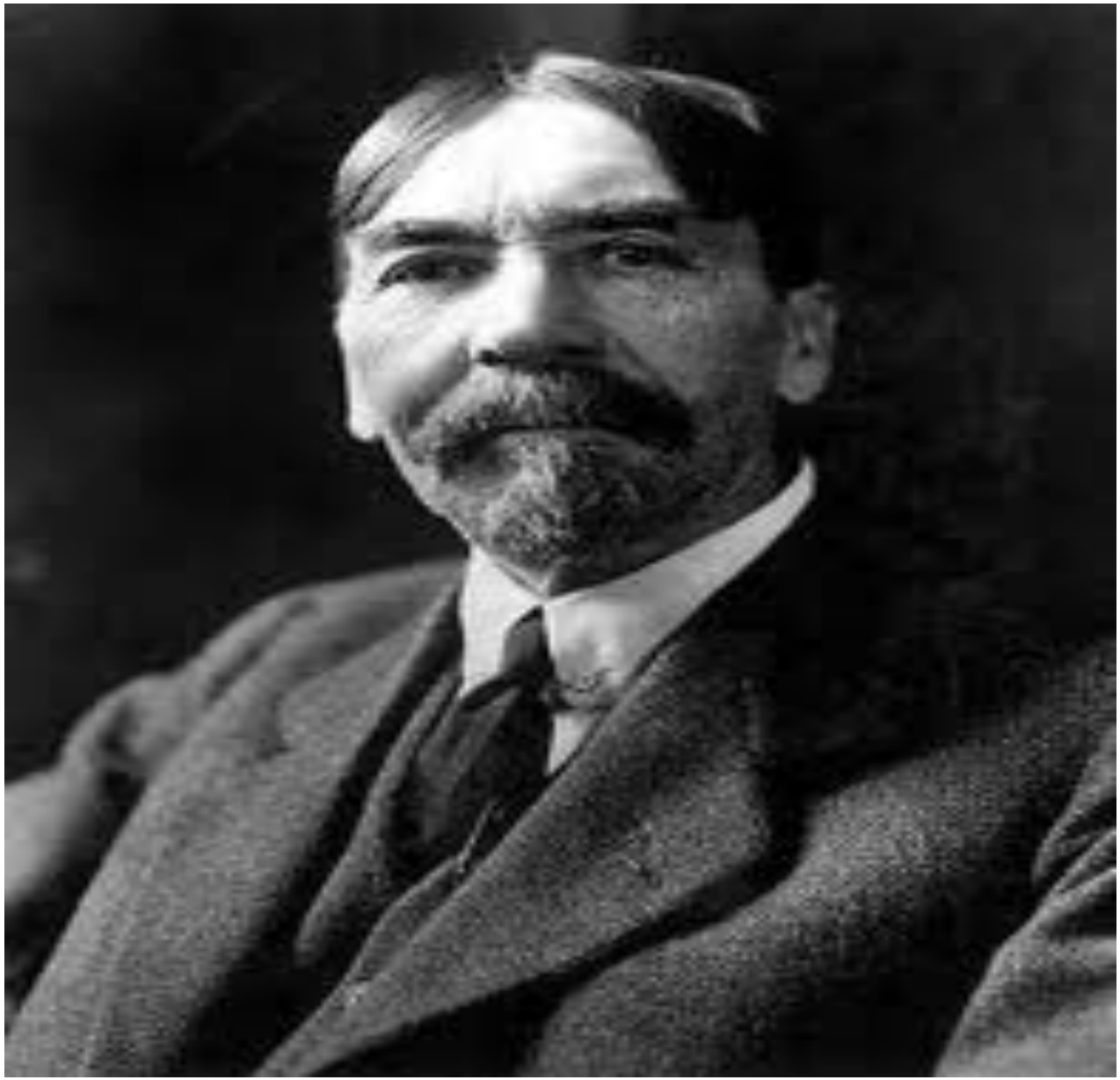


Characteristics of high-quality activities

- new knowledge with high market value
- steep learning curves
- high growth in output
- rapid technological progress
- high R&D-content
- necessitates and generates learning-by-doing
- imperfect information
- investments come in large chunks/are divisible (drugs)
- imperfect, but dynamic, competition
- high wage level
- possibilities for important economies of scale and scope
- high industry concentration
- high stakes: high barriers to entry and exit
- branded product
- produce linkages and synergies
- product innovations
- standard neoclassical assumptions irrelevant

Characteristics of low-quality activites

- old knowledge with low market value
- flat learning curves
- low growth in output
- little technological progress
- low R&D-content
- little personal or institutional learning required
- perfect information
- divisible investment (tools for a baseball factory)
- perfect competition
- low wage level
- little or no economic of scale /risk of diminishing returns
- fragmented industry
- low stakes: low barriers to entry and exit
- commodity
- produce few linkages and synergies
- process innovations, if any
- neoclassical assumptions are reasonsable proxy



Thorstein Bunde Veblen (1857-1929)

Separating ‘good greed’ from ‘bad greed’.

‘The private interest of each individual, *when it coincides with the public interests*, is always the safest guarantor of public happiness’

Pietro Verri, Italian economist, 1771.

Veblen's Legacy

The institutional and evolutionary tradition of Veblen and his followers lasted well into the post-WW II period.

The last influential Veblenian was Arthur F. Burns, Chairman of the Federal Reserve until 1979. Burns was a student of Veblen's most influential student, Wesley Clair Mitchell.

Minsky Moments

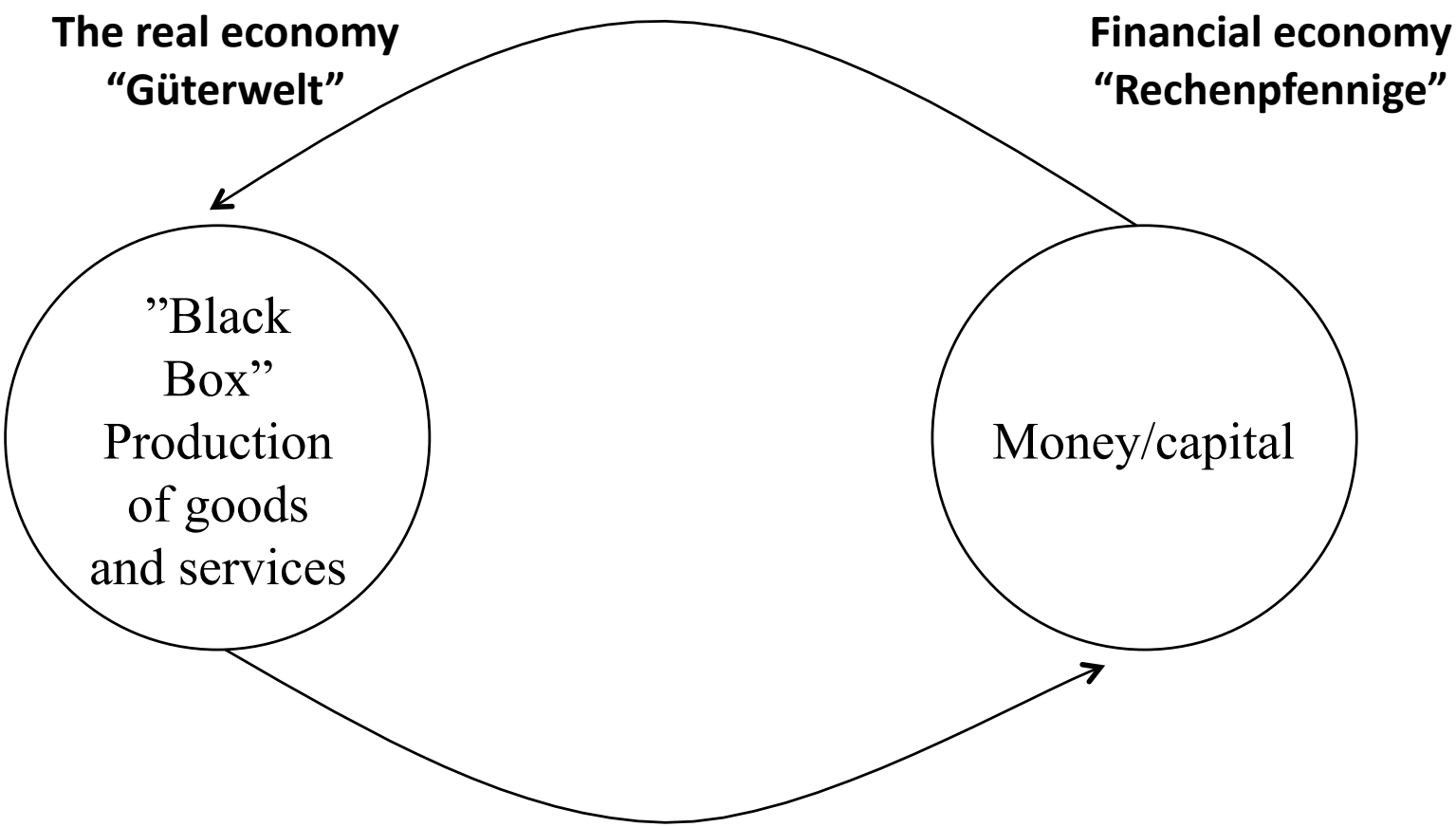
When everyone understands that the stock market (bond market) will collapse

Veblen Moments.

When everyone understands that most of the serious money which is being made, is made in ways which do not contribute to innnovation and increasing living standards.

Money is instead made through predatory activties: speculation and/or «sabotage» (= conscious withdrawal of efficiency).

The Circular Flow of Economics



Finanssektor : 17899

Realøkonomi : 00000

Europe's response: Good intentions

In the 42 points of the European Council Conclusions on the Stability and Growth Pact and the Lisbon Strategy from 2005, the underlying problems of the present situation of Europe are not raised.

The discussion appears as a long list of good intentions which – it seems implicitly to be assumed – necessarily will lead to success. The Lisbon Strategy appears to have been superimposed on the neo-classical economic framework dominating in the 1990s, where the market is a great equalizer and creator of economic order and harmony.

Three Times Rise and Fall of ’Physics-based’ Economics

School	Starting point	Peak	Death
Physiocracy (’Rule of Nature’)	Quesnay 1758	1760s	1789
Classical Economics	Ricardo 1817	1840s	1848
Neoclassical synthesis	Samuelson 1948	1990s	NOW

Forces set in motion:

- De-industrialization
- De-agriculturalization
- De-population

Examples; Southern Mexico, Moldova, Caribbean states, Latvia.

Destruction of real wages:

- In small Latin American countries from the mid 1970s.
- Stagnating wages in the US from about the same time.
- De-industrialization of The Second World starting in 1990 (from Latvia to Mongolia).
- Argentina late 1990s (real wages down by 40 per cent from peak) + Asian crisis.
- Western Europe is being hit now.

Mario Monti and Mario Draghi from Goldman Sachs are in Charge.

«Just print as much money as you want»

Financial Crises: A theoretical axis independent of right and left

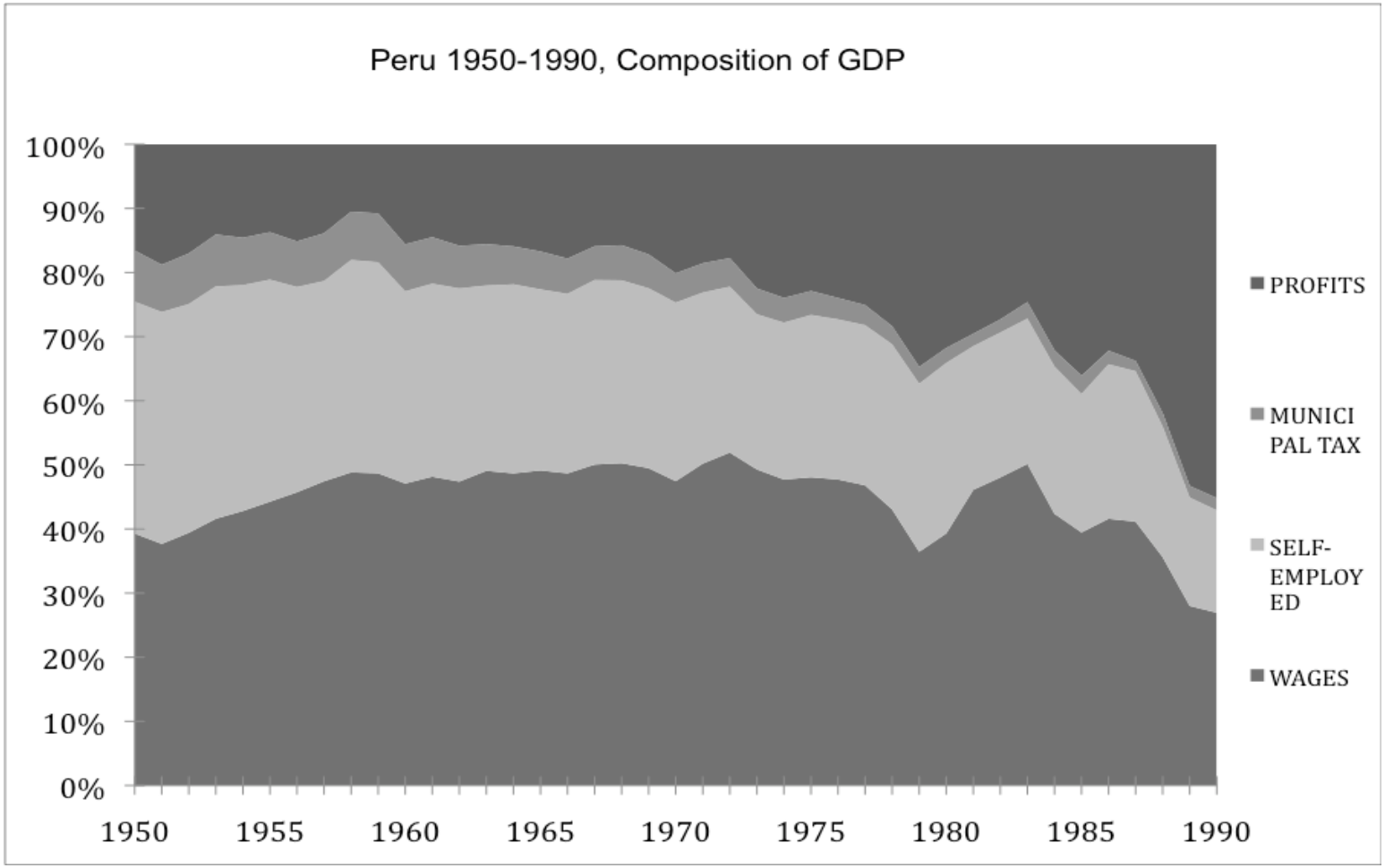
Financial crises a natural part of capitalism (Anti-physiocracy):

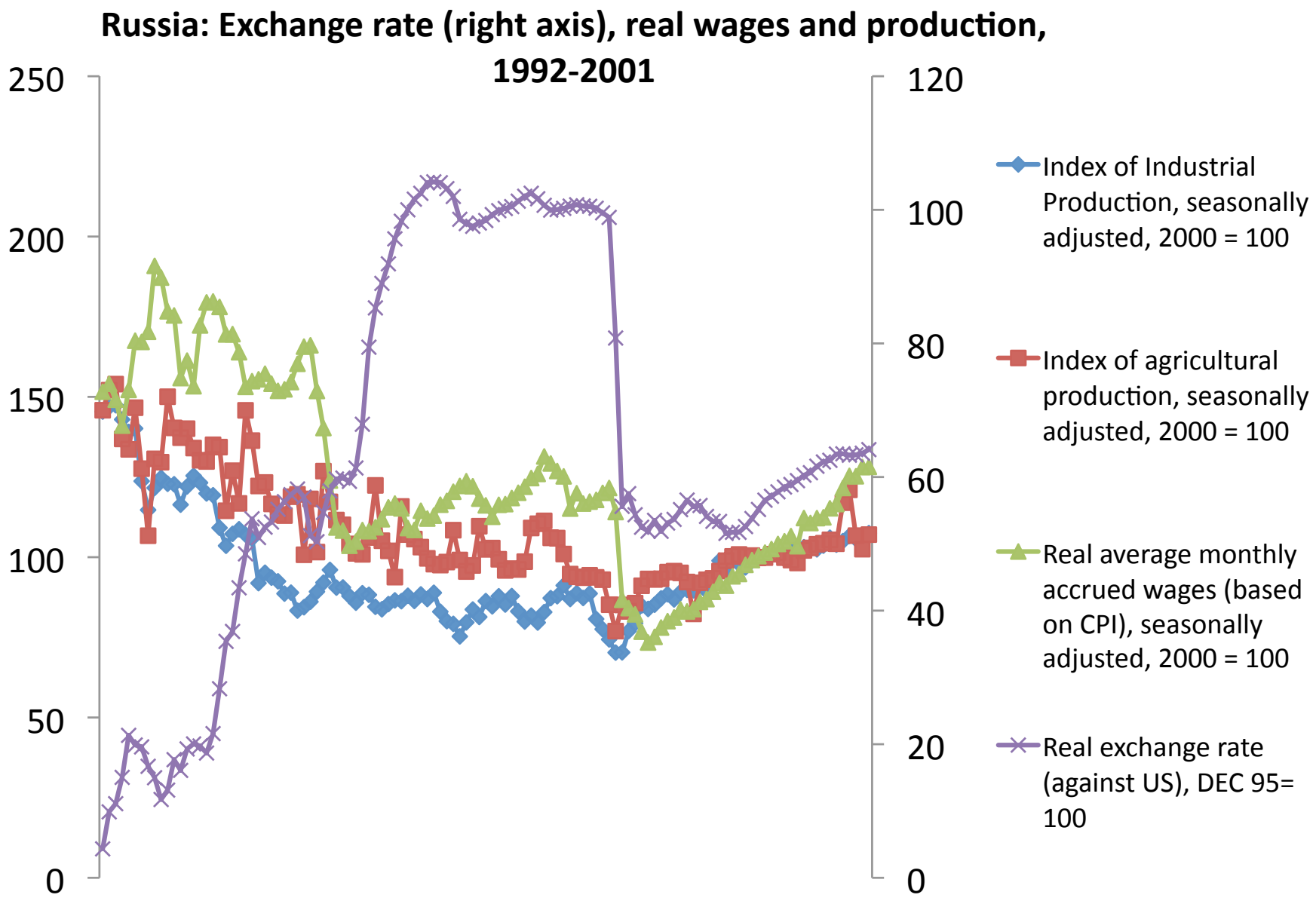
- Marx
- Lenin
- Hildebrand (Austria)
- Schumpeter
- Keynes
- Minsky

Fails to see financial crises (Physiocracy):

- Quesnay (French Revolution)
- Ricardo & followers
- Neo-classical economics + neo-liberalism

Peru: FIRE-sector and falling real wages as a percentage of GDP.




Russia: Exchange rate (right axis), real wages and production, 1992-2001
250
200
150
100
50
0
120
100
80
60
40
20
0
Index of Industrial Production, seasonally adjusted, 2000 = 100
Index of agricultural production, seasonally adjusted, 2000 = 100
Real average monthly accrued wages (based on CPI), seasonally adjusted, 2000 = 100
Real exchange rate (against US), DEC 95= 100

Thorstein Veblen's taxonomy of knowledge.

- **Esoteric knowledge**. Prestigious, but often fairly useless. Arises when education has 'contaminated' healthy instincts. Factless economics.

- **Exoteric knowledge**. Useful knowledge that carries little prestige. Fact- and experience-based economics.

Degenerate Learning (Bacon).

‘Surely as many substances in nature which are solid, do putrify and corrupt into worms, so is the propriety of good and solid knowledge to putrify into a number of subtle, idle, and unwholesome questions with no soundness or goodness of quality.

This kind of degenerate learning did chiefly reign amongst the schoolmen, who, being shut up in the cells of monasteries and colleges, and knowing little history, did, with no great quantity of matter, spin out unto us labourious cobwebs of learning that are admirable for their fineness of thread and work, but of no substance or profit’.

Francis Bacon, *On the Advancement of Learning*, 1605.

‘I think there’s a pretty good case to be made that the stuff that I stressed in the models is a less important story than the things that I left out because I couldn’t model them…’

Paul Krugman in *The New Yorker*,
March 1, 2010.

The Options of the West (compared to the 1700s):

Declining like Amsterdam: Relatively, no longer being number one, but keeping producton and finance in place.

Declining like Venice: Absolutely, losing first production and then finance, in the end becoming a museum.

THE American Plutocracy

BY

M. W. Howard,

Member of Congress, Seventh Alabama District.

Illustrations by A. A. COBB.

"Here, on the soil enriched with the blood of the patriotic dead, is to be erected an aristocratic monarchy, with wealth as its God."—*Wendell Phillips.*

NEW YORK.
HOLLAND PUBLISHING COMPANY,
1287 BROADWAY.

Holland Library No. 4. December, 1895.

6. Bengt-Åke Lundvall:
Why is the Northern Light Dimmin
in Europe. Some lessons from Denmark.

WHY IS THE NORTHERN LIGHT DIMMING IN EUROPE? SOME LESSONS FROM DENMARK.

Bengt-Åke Lundvall

Aalborg University

Seminar on the Industrial High Road to Sustainability and Growth at the Friedrich Ebert Stiftung ,

Stockholm

October 25 2012

My background

- Professor at Aalborg University, Denmark
- Four major research projects on Danish economy since 1980
- Deputy director of Directorates for Science, Technology and Industry at OECD 1992-95.
- Engaged as expert in preparing the Lisbon Strategy 2000.
- EU ambassador for Creativity and Innovation 2008.
- Secretary General for the global network on innovation and economic development Globelics (see www.globelics.org)

The message: The neglect of the *quality* of working life is a major problem for Europe!

1. 2000 the Lisbon strategy pointed to the creation of more and *better* jobs. This was never taken seriously and 2005 it was changed into just ‘more jobs’.
2. The difference in how people work and learn between different parts of Europe are quite dramatic. The euro-countries in crisis are those most exposed to competition from low-wage competition.
3. A major reason for strong performance of Nordic countries is that ordinary workers take responsibility and solve problems on their own.
4. This reflects an egalitarian society – the correlation between equality in working life and in income is close to 95%.
5. Now – driven by neoliberal economics and crude understanding of competitiveness – governments allow inequality to explode.
6. This is reflected in growing inequality in working life and in stagnating productivity. The Danish case as illustration.

The euro-crisis – the Lisbon Strategy and the EMU

- The Lisbon Strategy 2000-2010 knowledge based competitiveness with more social cohesion. More and better jobs.
- Two perspectives on the Lisbon strategy as Scaffolding for the EMU:
  - Upgrading the knowledge base of the South
  - Flexibilisation of the labour markets in the South
- Midterm evaluation marked (2005) a change toward the flexibilisation perspective.
- No more reference to better jobs or to social cohesion – in spite of increasing income inequality in most member countries.
- Flexicurity without security.
- Alternative would have involved massive investments in upgrading skills and jobs in the south – true flexicurity and broad-based education.
- *When Europe went Right it went Wrong!*

Table 1: National Differences in Organisational Models (percent of employees by organisational class)				
	Discretionary learning	Lean production learning	Taylorist organisation	Simple organisation
North				
Netherlands	64,0	17,2	5,3	13,5
Denmark	60,0	21,9	6,8	11,3
Sweden	52,6	18,5	7,1	21,7
Finland	47,8	27,6	12,5	12,1
Austria	47,5	21,5	13,1	18,0
Center				
Germany	44,3	19,6	14,3	21,9
Luxemb.	42,8	25,4	11,9	20,0
Belgium	38,9	25,1	13,9	22,1
France	38,0	33,3	11,1	17,7
West				
UK	34,8	40,6	10,9	13,7
Ireland	24,0	37,8	20,7	17,6
South				
Italy	30,0	23,6	20,9	25,4
Portugal	26,1	28,1	23,0	22,8
Spain	20,1	38,8	18,5	22,5
Greece	18,7	25,6	28,0	27,7
EU-15	39,1	28,2	13,6	19,1

Source : Third Working Condition survey. European Foundation for the Improvement of Living and Working.

Implications for the current Euro-crisis - on the need to do the impossible

- Common fiscal policy is a necessary but not a sufficient step if the aim is to make the current EMU-area sustainable in the long run.
- There is a need for a brodbased strategy aiming at building institutions that help upgrade industrial, innovation, education, labour market and social dimensions.
- What is actually needed is a Marshall-plan for the South – so far it is politically impossible!!
- Will the crisis expand what is possible??

Inequality of income and inequality in workplace participation in European countries 2000

More egalitarian economies are better off. One reason is broader participation in change – fundamental in the learning economy.

- In countries with high degree of income inequality (Portugal, UK, Spain, Greece, Portugal, Ireland) there are big differences in participation in organisational learning between Management and Workers.
- The inequality both in income and in participation is much less in the Nordic countries, Netherlands and Austria.
- In most sectors organisational learning is a prerequisite for turning innovation into economic growth. It is undermined by increasing income inequality.
- The inequality index is constructed by dividing the share of ‘workers’ engaged in discretionary learning by the share of 'managers' engaged in discretionary learning and subtracting the resulting percentage from 100.

	Income inequality Gini Coefficient	Ranking Income inequality	Inequality in 0rganisational learning	Ranking Inequality in 0rganisational learning
Austria	0.257	11	39.9	12
Belgiun	0.279	7	53.1	8
Denmark	0.225	15	35.9	15
Finland	0.246	13	37.9	13
France	0.278	8	61.9	6
Germany	0.275	9	43.8	11
Greece	0.334	4-5	57.9	7
Italy	0.334	4-5	67.3	2
Ireland	0.313	6	64.9	4
Luxemburg	0.260	10	52.9	9
Netherlands	0.231	14	37.3	14
Portugal	0.363	1	69.2	1
Spain	0.336	3	63.5	5
Sweden	0.252	12	50.3	10
UK	0.343	2	65.9	3

The rich get richer and the poor get poorer in Denmark 2001-2007

Tabel 2. Udvikling i disponibel indkomst opdelt på indkomstgrupper, 2001-2007

	Gennemsnitlig årlig realvækst i disponibel indkomst	Stigning i disponibel indkomst	Disponibel indkomst 2007
	Pct.	1.000 kr.	1.000 kr.
10 procent fattigste	-0,9	-4,4	81,5
2. decil	1,6	12,9	144,4
3. decil	1,9	17,9	170,1
4. decil	2,1	22,4	191,2
5. decil	2,2	26,1	210,4
6. decil	2,3	29,6	230,2
7. decil	2,4	33,2	252,2
8. decil	2,5	38,1	279,1
9. decil	2,6	45,2	317,2
10 procent rigeste	3,3	82,7	464,2
Alle	2,3	30,4	234,1

Anm: Da seneste data-år i registrene er 2007, er indkomstniveauerne kørt frem til 2010 med løn- og prisudviklingen for at give et billede af forbrugsmulighederne i 2010. Indkomsterne er husstandsækvivalerede, jf. boks 1. Kun 25-59-årige er taget med.
Kilde: AE på baggrund af Lovmodellens datagrundlag.

Finn Kenneth Hansen, CASA, Indkomstoverførsler og ulighed, Feb.2011

Increase in income inequality is reflected in weaker workplace participation

	2000	2005	2010	Comment
Denmark				The workplace participation indicator is the share of all ‘workers’ that are engaged in ‘discretionary learning’. The fall in Danish participation is dramatic and weakens its position as a learning economy
Gini	21	24	27	
Work	56	46	48	
Sweden				
Gini	22	23	24	
Work	38	56	34	
Finland				
Gini	24	26	25	
Work	39	38	31	
EU 15				
Gini	29	30	31	
Work	29	30	24	

The major factor behind weak competitiveness in Denmark is weak productivity growth

This is recognised by the most recent EU-report – May 2012. COMMISSION STAFF WORKING DOCUMENT- In-Depth Review for DENMARK in accordance with Article 5 of Regulation (EU) No 1176/2011 on the prevention and correction of macroeconomic imbalances

But the report has little to offer in terms of explanations. Not one word about growing inequality and change in worklife participation:

"While it has proven difficult to identify the factors behind the falling trend in productivity growth in Denmark and to come up with clear-cut policy conclusions, research results point towards a number of factors at play."

- Barriers to competition in Denmark.
- Weak conversion of R&D expenditure into marketable innovations
- Weak performance of education system

Why the Learning Economy is more adequate than the KBE

- The most important characteristic of the current economy is that success reflects capacity to learn.
- Rapid change makes knowledge obsolete and requires learning among employees and firms.
- This is why ’life-long learning’ and ’learning organisations’ should be seen as real concerns.
- Investments in Education and R&D should be assessed in terms of impact upon capacity to learn.

Summing up

Nordic countries have performed extremely well in a long term perspective.

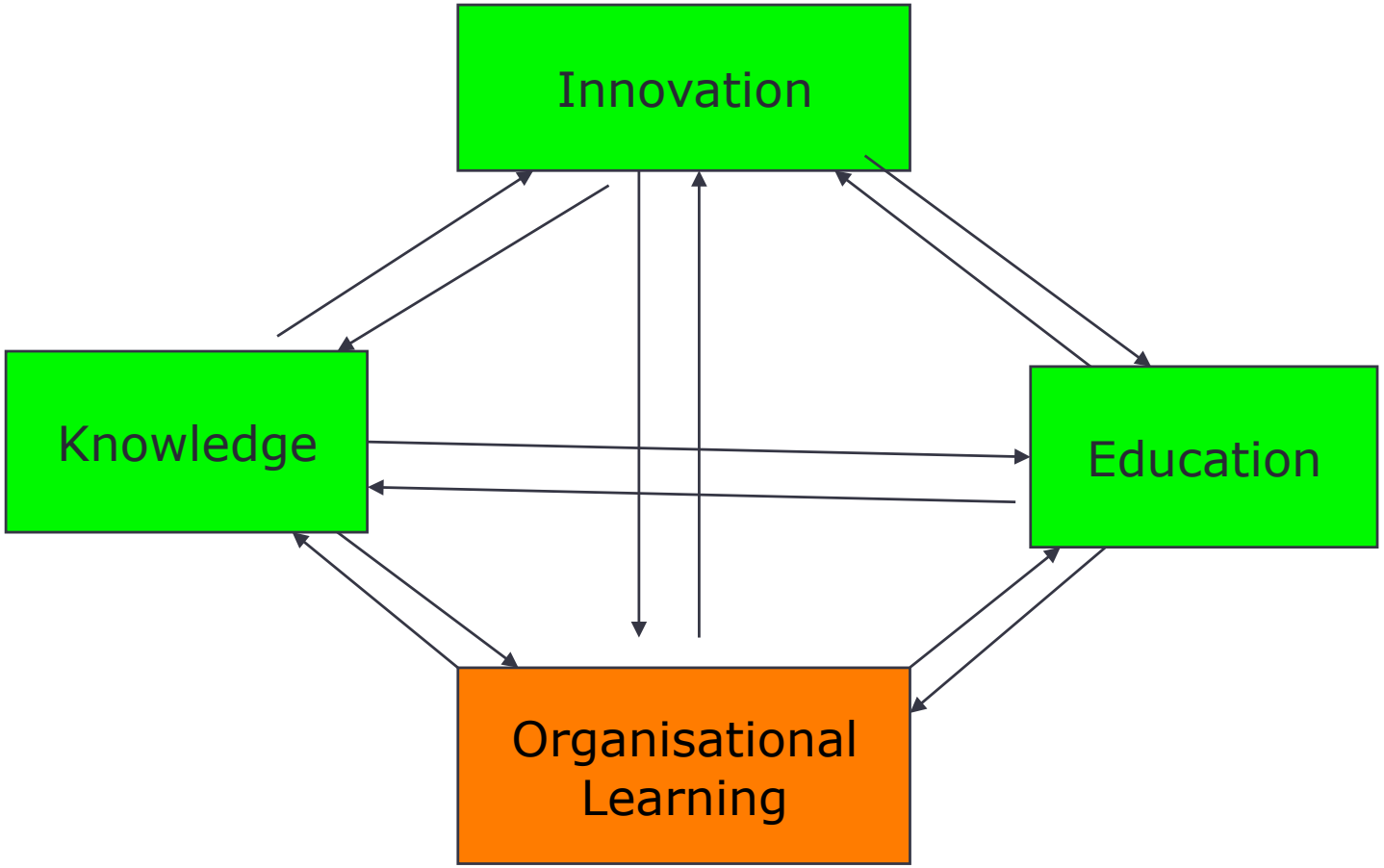
- High income level
- High on well being indicator
- Attractive for investment

- Core element of the Nordic Model is equality in income and status.
- This is reflected in working life where ordinary workers take on responsibility and solve problems on their own.
- This is a major reason for the strong performance in a globalising learning economy.
- When the basic equality erodes productivity stagnates

Implications for crisis solutions – the New New Deal

- Investing in R&D and formal education is not sufficient.
- Recommending reforms to expand supply of ’labour’ without considering the skill distribution of supply and demand is IRRESPONSIBLE!
- Redistributing the capacity to learn in favor of weak learners combined with egalitarian and solidaric income and tax policy creates the basis for broad participation in change in society.

From EU's Knowledge Triangle to the Knowledge Rectangle



- Thanks for your attention!

7. Charles Edquist:
Innovation Policy for Growth and Sustainability – Some Swedish experiences and the way forward

“Innovation Policy for Growth and Sustainability – Some Swedish experiences and the way forward”

Arena’s Economic Council
Friedrich Ebert Stiftung
October 25, 2012

Charles Edquist
CIRCLE, Lund University, Sweden

I will talk about:

1. The character and role of innovation policy

2. Some Swedish experiences

3. The way forward = the development of a holistic innovation policy for growth and sustainability – illustrated with the instrument of Public Procurement for Innovation (PPI)

What **is** Innovation Policy?

It is **all** actions by public organizations that influence innovation processes.

It **includes** actions by public organizations that **un**intentionally affect innovation.

This means that innovation policy is seen as "**superior"** to other related policy areas – This is possible to achieve with an **Innovation Policy Council** chaired by the Prime Minister.

Why innovation policy – not industrial policy?

- The economic and societal **importance** of innovations
- Innovations are not only industrial – also **intangible**, and also in the **public** sector
- Innovation policy is associated with **change, flexibility and the future**
- Industrial policies are burdened by support to **old and dying sectors**
- A future-oriented innovation policy is **practiced** in many countries, e.g. in Asia – with great success

Objectives of Innovation Policy

- The **ultimate** objectives of innovation policy are politically determined.
- They can be economic, environmental, social, related to health, related to defence and security, etc.
- It is an important **political** issue how different ultimate objectives shall be balanced.
- But the ultimate objectives have to be 'translated' into **direct** objectives, i.e. into **innovation** terms – this is self-evident but rarely done.

Reasons for policy intervention

Two conditions must be fulfilled for public intervention to be motivated in a market economy:

(1) Private actors must fail to achieve the objectives formulated; i.e. a **'problem**' must exist. An **innovation policy problem** is a low innovation intensity for a certain category of innovations.

(2) Public actors must have the **ability** to solve or mitigate the problem.

Some Swedish experiences:

- The Swedish paradox
- Public procurement for Innovation (PPI)
- The National Innovation Strategy

The way forward (1)

It is necessary to develop a more specific strategy before it can be used for innovation policy action.

- Develop specific innovation policy objectives.
- Make sharp priorities – focus on **new** fields = be future-oriented.
- This implies that innovation policy shall serve as a **mid-wife** – not provide support towards the end of life! *(Framtiden har inga lobbyister = mid-wifes are needed!)*
- It is a matter of helping to create jobs in knowledge-intensive sectors in both industry and service production.

The way forward (2)

- Adapt a part of **existing** public policies in near-by policy areas so that they **enhance** innovations:
  - research policies, (35 billion Crowns = 1% of GDP!)
  - education policies,
  - procurement policies – (700 billion - see next picture),
  - regional policies,
  - entrepreneurship policies,
  - Framework policies (tax laws, rules about patents,)
  - Policies for public financing of early-stage innovations, Etc

- **Many hundred billion crowns** are yearly spent on these policy areas – 10% could be adapted to enhance innovation

- This **can** be achieved if the effort is coordinated from the Prime Minster's office in an **Innovation Policy Council**.

The way forward (3) – an example

- Regular public procurement in Sweden is about 700 billion Crowns – if 10 % of this is spent on **Public Procurement *for Innovation* (PPI) = 70 billion!**
- PPI affects growth and jobs (argued earlier), but they are not the **objectives of PPI**. The objectives are:
  - To satisfy human needs and/or
  - To solve societal problems
- Growth and sustainability are **compatible** as objectives of PPI
- PPI is also a means to **mitigate global challenges** (climate, energy, etc) – a substitute for the break-down in climate negotiations

10 Important determinants of innovations:

1. R&D
2. Education and training
3. Formation of new product markets
4. Articulation of quality requirements
5. Creation and changing organizations
6. Interactive learning
7. Creating and changing institutions
8. Incubation
9. Financing of innovation processes
10. Consultancy services

Note: Innovation policy is **not** one of the activities. It is a part of **all** the activities.

In **practice**, a **holistic** innovation policy **is** public intervention with regard to **all the ten activities**.

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charles.edquist@circle.lu.se

www.circle.lu.se