We Need An Industrial And Innovation Policy For Europe

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The prolonged economic crisis since 2008 has drastically reduced incomes and employment levels and the promised recovery will not reabsorb unemployment, particularly in Europe. Nevertheless, economic policy in Europe is sticking to past recipes based on two mainstays: fiscal austerity and labour flexibility. This strategy does increase the short-run cost competitiveness of European firms overseas but this comes at the cost of decreasing the size of European internal markets reliant on domestic demand.

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Europe needs clearly structural reforms, but of a kind very different from those asked by the European Commission during this crisis.

We here report on two closely connected and integrated lines of policy intervention related to the labour and the industrial system in Europe and its periphery countries. The two layers of intervention relate to industrial/innovation policy and labour policies mainly linked to wage setting.

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Industrial And Innovation Policy

First of all, Europe needs a public industrial policy for strategic sectors, both traditional and mature, new and innovative. This policy must be complementary to government macro policies aimed at sustaining aggregate internal demand that private firms view as seriously deficient. Such demand can be increased only by stepping up public expenditure on investments – a strategy that requires major changes in the Eurozone's Fiscal Compact.

Establishing an effective industrial policy means:

- choosing how and where to place national manufacturing in the global market in terms of technology, production and demand, and
- backing structural changes in the economic system, not only quantitative growth in demand but changes in its composition and direction.

Stronger investment depends on the removal of budgetary constraints imposed on Eurozone countries so action has to take place at a pan-European level if industrial policy is to be more than just a rhetorical flourish.

Europe should also be the arena for an effective industrial renaissance. Product innovation has a large, positive direct effect on employment; the same does not hold for process and organizational innovations. But the latter innovations usually have a positive impact on a firm's economic performance and hence on product innovation as well.

Choosing which key sectors and research areas public actors should invest in is closely linked to policies that aim to spur innovation in the private sector.

Secondly, it is time to establish a government policy that fosters not only traditional technological innovation but induces the adoption of best work organization practices. These should be focussed on labour organisation changes with worker participation in decision-making at shop floor level.

To this end various tools should be designed:

- innovation policy requires an active role for public actors to direct and guide government investment at the European level.
- particular attention here should be paid to the employment intensity of investments.
- specific policies could help innovate by increasing employee participation in firms' decision-making, improving their responsibilities and autonomy, reducing hierarchical levels and increasing problem solving behaviour.

Innovation policies must not only spur R&D or technological development but also prompt firms to introduce organizational innovations adopted in bundles aimed at increasing productivity – particularly in periphery countries.

Wage Policy

The role of wage determination is crucial within this integrated industrial and innovation policy. The rationale behind wage-setting should point to a new dynamic favouring growth, combining employees involvement and innovation.

Here we recognize the importance of renewing the role of national bargaining in the two-tier system:

- At national level, wage increases should be negotiated in the first place in order to preserve purchasing power.
- At this national contractual level, higher wages should not simply be treated as a residual leftover for firms to decide.

The social parties and government should adopt measures designed to reach a targeted growth in productivity by acting on technological and organizational innovation, investment in physical and intangible capital, using public resources to spur R&D, encouraging public and private investment to improve human capital, reducing working time.

- Bargaining at the second, decentralised level should employ specific measures to attain productivity and wage increases.
- At this level, the adoption of a pay-for-participation model would imply that wage increases are linked to organizational changes and to a commitment to technological innovation, product and process innovation, ICT development, improving human capital empowering and environmental innovations. This new pay-for-participation model would help encourage employees to embrace new ways of organizing work and generate incentives to innovate in several spheres.

This policy would, what's more, reduce the aberrant separation between *productivity* and *real wages* that several European economies have experienced in the last decade – contributing to reducing labour income's share of the economy and depressing aggregate demand via compressed consumption. The proper route would be that of a "golden rule for wages" in which real wages increase at the same pace as productivity. Eurozone labour policy should monitor wage movements in individual countries in accordance with their internal and external imbalances.

Those countries showing a large trade surplus and fast productivity growth should increase real wages at a faster pace than productivity. The combined effect of extra domestic consumption and increased unit labour costs would help to reduce the trade surplus. Countries with slow productivity growth and a trade deficit should use the real wage dynamic as an instrument to increase productivity and recover competitiveness. The latter must be achieved through innovation and not via wage deflation, with real wage rises tied to productivity goals set nationally by the social parties and government.

Conclusion

Current policies in Europe and particularly in periphery countries – pursuing fiscal consolidation at all costs – have effects at odds with the desired ones. We see cuts in employment rather than job-creation; firms take advantage of bargaining against an even weaker counterpart (the unions): higher flexibility and a squeeze on wages are the result, with a further depressive effect on consumption and thence on aggregated demand. Nationally, we are forced to act within binding rules agreed at EU level.

It is at this European level that we need the biggest change. The Fiscal Compact urgently requires major revisions. And coordinated labour policies among Eurozone countries should follow the “golden rule for wages” of fostering wage-led growth rather than one that is export-led – and based on labour market flexibility and consequent wage deflation.

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