



creating
sustainable growth
in europe

**Midpoint Policy Debates
Summary Report**

Auswärtiges Amt, Berlin
November 2007

Foreign & Commonwealth Office, London
December 2007



A policy research initiative from the

Anglo-German Foundation
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This report summarises the speeches, presentations and discussions from the two policy debates held in November and December 2007 in Berlin and London to mark the halfway point of the Anglo-German Foundation's research initiative *creating sustainable growth in europe*.

The event in Berlin was hosted by Martin Kobler, Director, Culture and Communication, on behalf of the Auswärtiges Amt, and chaired by the journalist and consultant Heik Afheldt. The London event was hosted by Anthony Smith, Director European Political Affairs, on behalf of the Foreign & Commonwealth Office, and chaired by Stephanie Flanders of the BBC's *Newsnight*. Our thanks go to all those who contributed, whether from the podium, from the floor, or from behind the scenes.

More information on the initiative, including the papers presented at the research conference held in Berlin following the policy debate there, can be found at: <http://www.agf.org.uk/currentprogramme/CreatingSustainableGrowthInEurope.php>

The four research programmes that make up the *csge* initiative will finish their work during the first half of 2009. A series of publications and dissemination events will launch the findings into the public policy debate.

If you wish to receive further publications emerging from the initiative, or invitations to dissemination events, please subscribe at: <http://www.agf.org.uk/subscribe.php>



Ray Cunningham, Director of the Anglo-German Foundation;
Tony Atkinson, Chair of the *csge* Academic Advisory Board

Foreword by Tony Atkinson

The world is changing rapidly, and so also are the two countries – Germany and the United Kingdom – that established the Anglo-German Foundation in 1973. At the time the Foundation was created, the United Kingdom had only just become a member of the European Communities, joining the six founder member states. Berlin, the city where the first policy debate was held in 2007, was in 1973 divided by the Wall. The world then was divided politically and economically. Today, the world is very different. The European Communities have become the European Union, with 27 member states. The Soviet Union is no more. China, Brazil and India are becoming major economic powers. It is therefore not surprising that the Anglo-German Foundation has decided that its founding purpose – promoting the exchange of knowledge, ideas and best practice between the two countries – has been well served and that the great majority of its remaining resources should be devoted to a major research initiative on *creating sustainable growth in europe (csge)*.

The responsiveness of the Foundation to changing circumstances served as a leitmotif for the midpoint debates held in November and December 2007 in Berlin and London. The key issue policy-makers and individual citizens face is how to adapt to a changing world in a way that preserves the essential qualities of our societies. This will involve institutional change, and such change is inevitably disruptive. It will involve major shifts in our lifestyles, and the burden of adjustment needs to be shared fairly. In achieving the necessary change, a key role will be played by research. All four programmes that make up the *csge* initiative are contributing to our understanding of the problem of reconciling the desire for growth with environmental and social sustainability.

In highlighting environmental and social sustainability several years ago, when the initiative was launched, the Foundation was ahead of the public debate. Before the Stern Review, before Al Gore and the Nobel Peace Prize, the *csge* initiative had identified the need to bring together research on environmental sustainability with the mainstream debate about economic growth. With today's heightened awareness, it is scarcely surprising that the debates in Berlin and London were dominated by this issue. Both Professor Dr Troge, President of the Umweltbundesamt, and Jim Murphy, the UK's Minister for Europe, stressed the importance of the new EU targets and of the EU's emissions trading scheme.



Stephanie Flanders

Environmental issues were prominent; but I came away with a sense that we had not really grasped the macro-economic nettle. It is true, as pointed out in the panel discussions, that technological development and increased output are needed to improve environmental protection, but it seems increasingly clear that there has to be a reduction in consumption in rich countries. Gross domestic product will continue to grow, but a larger proportion has to be invested and allocated to environmental protection, and a much larger proportion transferred to others. Or, put differently, there has to be a redistribution of current total consumption among the citizens of the world. Sustainability at a global level can only be achieved if we address at the same time the longstanding issue of securing more even global development.

Achieving such a shift in macro-economic policy is a lot to ask of the governments of Germany and the United Kingdom, or of any country. How can the research of the csge initiative contribute? Here I will highlight just two themes that emerged from the conferences. The first is the integration of economic and social policy. Too often in the past these have been treated as unconnected. Economic policy is the responsibility of the financial and business ministries; social policy is determined by the spending ministries. But issues such as pensions have to be seen as an integrated whole. Pensions are not just relevant to macroeconomic stability but affect the lives of most of us. Moreover, in the debate about future consumption levels, pensions form a key part of any intergenerational compact. As the EU develops a common immigration policy, the design of the policy has to take account in a unified way of the implications for the labour market, for the macro-economy, for social cohesion, and for the environment. When we discuss the introduction of environmental taxes, we have to consider their distributional burden. Sustainability is a social as well as an environmental concern.

The second theme is the identification of the key actors. The mission of the Foundation is to contribute to the policy process and to encourage exchange between researchers and practitioners. Over the past 35 years, the policy process has changed. The EU is now a leading world player, and, for all the inherent difficulties in making decisions with so many member states, is increasingly providing the locus for policy formation. And power has also shifted downwards, with increased responsibilities being assumed by regional or local governments. In this respect, the United Kingdom today looks more like the Federal Republic of Germany.



Sir Michael Arthur, the British Ambassador, welcomes the guests in Berlin

But policy is not just made by politicians. Research on the csge initiative has emphasised the key role of managers, and the role of social partners and of families. We need to understand better the mechanisms by which change is determined and facilitated.

On these issues, and on the subject as a whole, we look forward to the full and final results of the csge initiative.

The Academic Advisory Board of csge, which I chair, has been involved in the selection and development of the research programmes, and I would like to end by thanking the members of the Board for their helpful and constructive participation.

The members of the Academic Advisory Board are:

- Professor Sir Tony Atkinson, Nuffield College, University of Oxford (Chair)
- Professor Lars Calmfors, Stockholm University
- Professor Wendy Carlin, University College London
- Professor Roland Clift, University of Surrey
- Professor Dr Anita Brigitte Pfaff, University of Augsburg
- Professor Chiara Saraceno, Wissenschaftszentrum Berlin and University of Turin
- Professor Dr Udo Simonis, Wissenschaftszentrum Berlin



Debate in the Europasaal of the Auswärtiges Amt, Berlin

Opening speeches

Professor Dr Andreas Troge, President of the Umweltbundesamt (Federal Environment Agency) – ‘A New Deal for the economy, the environment and jobs’

(Professor Troge stood in for Staatssekretär Matthias Machnig, Bundesministerium für Umwelt, Naturschutz und Reaktorsicherheit [Federal Ministry for the Environment, Nature Conservation and Nuclear Safety], who was detained on parliamentary business.)

Launching the Berlin event, Professor Troge focused on the interdependence of sustainability, economic policy and technology: ‘Ecological progress cannot be achieved without economic success. Equally, sustainable economic growth depends on us solving the dramatically increasing environmental problems.’

Drawing a parallel with Roosevelt’s New Deal in the 1930s, he argued that the urgent task confronting us is to mobilise in order to prevent the threatening world climate crisis. He identified several ‘megatrends’ that will intensify the ecological challenges:

- increasing industrialisation, technological innovation and the liberalisation of world trade
- world economic growth, which will increase by an average 3 per cent per year until 2030, with the Chinese, Indian and Indonesian economies becoming the motors of growth
- increasing population growth and urbanisation – by 2050 the planet will have to support 9.2 billion people, over half of whom will be living in Asia.

All this, along with ever-growing demand for goods and services, means that greenhouse gas production could double by 2050, pollution will increase, and mineral resources will become increasingly scarce.

According to Sir Nicholas Stern, the cost of doing nothing about climate change will be at least 5 per cent of annual global GDP – possibly 20 per cent and more. Climate protection measures, by contrast, will cost just 1 per cent of annual global GDP. So action is essential now to use the current favourable conditions to build a new deal for the environment, the economy and employment.



Andreas Troge

The EU made historic decisions during the German presidency:

- to reduce greenhouse gas emissions by at least 20 per cent by 2020, rising to 30 per cent if other industrial economies achieve comparable reductions
- to significantly increase energy efficiency by 20 per cent by 2020
- to treble the use of renewable energies, also by 2020.

The target of a 30 per cent CO₂ reduction is ambitious but achievable and demonstrates that the time for incremental change lies in the past. If the EU’s target does rise to a 30 per cent reduction, then Germany, which is Europe’s biggest emitter, has set itself a very specific challenge – to reduce its emissions by 40 per cent compared with the 1990 level.

Climate change is not the concern of the state alone. Business and industry, agriculture and consumers all have vital parts to play. Professor Troge outlined some of the measures needed and underway in Germany. The public sector must use its purchasing power to promote energy-efficient technologies; older buildings must be upgraded to halve their energy consumption; the use of renewable energy sources must increase; fuel-consumption standards must be developed to encourage the use of energy-efficient vehicles; and a bonus system must be introduced to encourage energy-saving through cogeneration in industry. On the plus side, new environmental technologies and services present an enormous market opportunity. The worldwide market is expected to more than double by 2020, bringing with it increasing employment – the German environmental technology sector is already employing 13 per cent more workers each year.



Debate in the Locarno Suite at the Foreign & Commonwealth Office, London

This New Deal is for the environment, the economy and for employment. It will make demands on everyone. But it will also bring benefits all round with:

- new opportunities for growth
- new jobs in environmental technologies
- greater security of energy supply with less dependency on foreign energy sources
- improved trade balances because of reduced energy imports
- more social justice, because, if action is not taken to reduce emissions, the high prices of raw materials would hit low-income groups disproportionately
- reduced potential for international conflict, given the strategic importance of ensuring energy supplies and – of course –
- a better climate because of reduced greenhouse gas emissions.

However, a New Deal confined to Germany is not enough. Our biggest political challenge is to build a comprehensive global pact. Climate protection is a matter of global justice that cannot be reduced to mere ‘burden sharing’. The German New Deal, with its economic, ecological and social dimensions, must lay the foundations of a new global development model.



Jim Murphy

Jim Murphy, Minister for Europe, Foreign & Commonwealth Office – ‘A New Deal for Europe’

In London one week later, Jim Murphy also looked back to Roosevelt’s New Deal, as well as to the UK Labour government’s New Deal in 1997, when he called for a ‘New Deal for Europe’ that would ensure our continued success. ‘We need a New Deal to create more jobs, to look outwards to the rest of the globe, addressing our shared responsibility for climate security and driving forward the transition to a low-carbon global economy. This is our vision of a global Europe – a Europe which is built on openness, fairness, equality and co-operation.’

While national governments will drive the creation of more just societies across Europe, the EU has an important role to play. ‘Just as it has in climate security, the EU must lead by example in its commitment to free trade and open markets. A vibrant European economy will reward hard work; it can create opportunity for all whatever their background; it can alleviate poverty and need; and it can meet the rising aspirations of today’s young Europeans.’

One common national-level challenge is that of an ageing and shrinking workforce. ‘We cannot afford the levels of unemployment and inactivity that plagued the UK in the 80s and still exist in parts of Europe.’ Unemployment among young people, lone parents, the over 50s, and people with disabilities has already been tackled. Now the UK government needs to address poverty – both financial poverty and poverty of aspiration. Jim Murphy argued that we need to see welfare systems as an active tool of inclusion to help people get back on the ladder of opportunity. This means giving every child the opportunity to develop the full range of their talents, and every adult a second chance to develop their skills.

‘At a European level, the Lisbon Agenda is a ten-year strategy to create opportunities for Europeans. It is a strategy to create better jobs, wealth and lifelong skills.... A strategy that isn’t about majority votes or the jobs of Commissioners, but the careers of our citizens. About raising skills and aspirations, about Europe becoming once again the global centre of innovation and research.’ As part of this we need to review the long-term requirements for skills across the EU and to target social spending where it does most good in order to compete in the new knowledge-intensive global economy.



Panel members Soskice, Kretschmer, Flanders, Ekins and Clasen

‘The economic evidence tells us that, momentous as the challenge of climate security is, meeting it is both technologically feasible and economically rational. Europe can show that economic success and climate security are compatible. We can use the biggest rules-based market in human history to create important markets for innovative goods that reduce energy consumption. We can trade carbon and we can take action to make radical cuts in European emissions.’

‘The emissions trading scheme is already the model on which a global carbon market is being built. Can we also provide the policies, finance and innovation to deliver the other elements of a low-carbon, high-growth future? Our climate security is as strong a factor of wellbeing as job security and a strong social framework. Europe needs to work on delivering all three of these elements.... In truth, you can’t have social justice or economic success without climate responsibility. These things are linked. And it is through strong economic and environmental policies that we will forge a new deal for Europe. A new era of social justice and global responsibility.’

The full text of the Minister’s speech can be read on the Foreign & Commonwealth Office website at: <http://www.fco.gov.uk/servlet/Front?pagename=OpenMarket/Xcelerate/ShowPage&c=Page&cid=1007029391629&a=KArticle&aid=1196169267679&year=2007&month=2007-12-01>

The csge programmes

At each debate, the co-ordinators of the four programmes that make up the *creating sustainable growth in europe* initiative outlined the main themes of their work.

Professor Tobias Kretschmer: Explaining Productivity and Growth in Europe, America and Asia

This programme investigates why European productivity growth has been so disappointing over the last decade. This is a key issue for UK and German governments hoping to deliver the growth essential for funding improved public services and increasing employment. The evidence from analyses of the US ‘productivity miracle’ since 1995 shows that management practices, information technologies and innovation play central roles. The programme also investigates the environmental impact of the race for productivity growth. Is there an inevitable trade-off between higher productivity and a deteriorating environment or are there many ‘win-win’ policy scenarios in which environmental efficiency can be combined with productivity improvements?

The first key question is therefore: ‘What accounts for Europe’s slower productivity growth and what can be done to improve it?’ The hypothesis is that the management of European firms plays an important role and has hampered their ability to innovate, to exploit new IT technologies, and to react to the challenges of globalisation. The programme is carrying out the first rigorous cross-country empirical analysis of these factors, and is assembling a range of current and new datasets across Europe, America, China and India.

Of course, conventionally measured growth is not always desirable, and there may be damaging consequences for the environment. Indeed, increased industrialisation has exacerbated a number of unsustainable environmental trends including climate change, the detrimental effects of industrial waste, and the excessive exploitation of natural resources. The second key question is therefore: ‘What policies can help foster environmentally friendly productivity growth?’ The hypothesis is that there is no cast-iron law that there has to be a trade-off between productivity growth and the environment, and that many creative ‘win-win’ situations may exist. For example, better managed firms may promote both higher productivity and better environmental protection.



Panel members Kretschmer, Afheldt and Ekins

Professor Paul Ekins: Resource Productivity, Environmental Tax Reform and Sustainable Growth in Europe

By linking the concepts of resource productivity and environmental tax reform (ETR), this programme is generating substantial new insights into the conditions for environmentally and economically sustainable growth and how it might be promoted through public policy. The programme contributes at a European level to the joint pursuit of the Lisbon Strategy and the EU Sustainable Development Strategy.

The programme addresses the long-term relationships between energy, resource prices and resource use in the context of environmental quality, economic growth and competitiveness. It examines the effects to date of ETRs on employment, economic growth and competitiveness, and looks at the medium-term implications of these reforms in the UK and Germany for national, European and global economies. In highlighting these implications, it hopes to answer the crucial question of whether ETRs can increase growth and employment while at the same time reducing local and global environmental impacts. This, in turn, will give pointers for the design of future ETRs for EU member states, both old and new.

Uniquely, the programme will create a comprehensive comparative analysis of ETRs and their economic and environmental implications for the EU (also eastern Europe) and globally. It will analyse how ETRs might be able to address three areas of market failure in Europe:

- high unemployment in some countries
- a tendency to overuse common resources such as clean air and water
- underinvestment in new technologies.

This can be done by increasing the costs of using common resources, and by using the revenues raised to reduce labour costs and to subsidise the development of new resource-saving technologies.



Panel members Soskice, Kretschmer and Flanders

Professor David Soskice (co-director, together with Professors Stephen Machin and Christian Dustmann): The Economics and Politics of Employment, Migration and Social Justice

This programme asks key questions about how institutions contribute to inequality. While inequality has risen sharply in the UK and the US over the last two decades, research in the programme shows that it also grew to some extent in (West) Germany. The programme examines how, alongside earnings inequality, educational outputs and punishment and imprisonment may amplify inequality. It analyses the interdependent roles of different institutions (political, educational, criminal justice, collective bargaining) and social, demographic and economic factors in helping or hampering inequality. Some examples:

- When did wage inequality in Germany start to increase? The conventional answer is during the 1990s. This is being challenged by compelling evidence that wage inequality increased during the 1980s, though only above the median, and continued to increase both above and below the median from the early 1990s onwards. Skill-biased technological change increased inequality at the top of the distribution, while events such as the weakening of institutions were responsible for inequality at the low end of the distribution.
- Do unemployment benefits increase or decrease geographical mobility of labour? The theory so far is that, on the one hand, unemployment benefits decrease mobility, acting as a disincentive to job-search, but, on the other hand, may increase mobility by providing more resources for job-hunting. Evidence from cuts in the entitlement period in Germany in 1997 suggests that a longer entitlement period decreases mobility and the likelihood of finding a job.
- What impact does early school tracking (at age 10) have on student outcomes? The theory is that tracking may make schooling more targeted and effective. However, tracking may misallocate gifted but socially disadvantaged students. Research on different tracking regimes in England and Northern Ireland and on administrative data for Germany is finding that tracking misallocates immature students, but that institutional flexibility may correct this misallocation.



Panel members Ekins and Clasen

Professor Jochen Clasen: Sustainable Welfare and Sustainable Growth – Towards a New Social Settlement in Germany and the UK

This programme analyses, with a particular focus on issues of sustainability and social justice, the socio-economic challenges to the German and British welfare states and the ways in which traditional forms of welfare provision are adapting. For example, within family policy, the programme investigates how changes in family forms (demographics, household formation, care patterns) can be reconciled with public policies aimed at maximising the labour market participation of parents (child care, education, work-life balance). The programme is investigating how far companies might take greater responsibility for pension provision in ways that would contribute to income security in old age for many, not merely for some employees. The ‘social sustainability’ of welfare provision also includes political dimensions. For example, how far are new pension arrangements sustainable from the perspective of middle-income groups (as taxpayers) or employers (as pension providers)?

In relation to social justice, how far do the normative orientation towards social justice, the role of the state in social protection, and traditional notions of social solidarity correspond with current policies designed to bring about a greater mix of welfare providers and a stronger role for market-based principles? Whether median voters accept or support reforms is important, given that the legitimacy of welfare state reforms largely relies on the sustainability of social solidarity as a resource for a new welfare policy mix.

Family policy is being investigated in two further areas: changes in family forms (demographics etc) and family behaviour and preferences (employment and care work patterns, household structures), and also changes in family policy (changing policy orientations, actors and priorities). This work should reveal how far trends in these two domains are compatible or could create tensions. Work in early childhood education and care policy is similarly revealing potential frictions.



This picture and the following: contributions from the floor

Points from discussion

In both Berlin and London the large audiences of invited experts engaged in wide-ranging debate following the formal presentations. Some highlights from these discussions are summarised here.

Is it too late?

Audience comment

The very title of the AGF’s research initiative assumes that the huge reductions required in carbon emissions are compatible with economic growth. Time is running out for delivering a habitable planet to the next generations, and the only way to solve the problem is to cut emissions throughout the populated world.

Panel response (led by Professor Kretschmer)
[In theory economic growth can take place without having a negative environmental impact. And without economic growth we are unlikely to achieve the technical developments needed to improve environmental protection.](#)

How can we cost environmental impact?

Audience comment

Traditional accounting fails to recognise the environmental impacts of market activity. We need to develop a system of ecological pricing, whereby prices of goods and services reflect, at least approximately, the environmental impact they create.

Panel response (led by Professor Ekins)
[Sustainability has social justice dimensions as well as economic. Combined indicators that incorporate sustainable, environmental and social variables could be used as a second trend line in measuring GNP.](#)

Is a carbon tax all we need?

Audience comment

Using the Stern Review’s calculations on a) the costs of temperature stabilisation (1 per cent of world GDP) and b) the upper limit of CO₂ concentrations allowed if the temperature rise is limited to 2 degrees to cost emissions, we reach a price per tonne (€ 30) for allowances to ‘save the planet’. The ability of the atmosphere to accept greenhouse gases is a scarce resource, and should be priced accordingly. Pricing in this way is sufficient – other forms of regulation are unnecessary.



Panel response (led by Professor Ekins)

Markets themselves do not price carbon. Only government action can achieve a sustained higher carbon price. The price instrument is not as effective as it could be, and all governments have found it hard to create effective environmental tax measures. For example, in economic terms it would not cost much to implement Stern's argument that deforestation should be reduced in order to cut carbon emissions. However, deforestation's complex and strong social, economic and cultural drivers make it politically very difficult to reduce. In addition, it can be argued that in a democracy it is neither possible nor morally permissible to implement a radical policy of this kind merely through the market mechanism of price-fixing.

Further audience comment

There are three main reasons why a simple carbon tax would be inadequate:

- No one knows what it would be.
- It would have to change year by year, since the first 10 per cent of carbon reductions will be easier and cheaper to achieve than the second 10 per cent, and so on.
- It would have to vary from state to state, which would hinder trading options between countries.

Panel response

If carbon damage increases each year, it would be rational to increase the carbon tax rate accordingly. Announcing the tax rate in advance would give business the certainty it requires. The emissions trading scheme is a second best. Overall, some political consensus is essential for a sustained higher carbon price.

Have we forgotten happiness?

Audience comment

We need to incorporate recent ideas about contentment and happiness into work on sustainable economic growth.

Panel response (led by Professor Ekins)

The correlation between growth and happiness is not clear. We need to identify the factors (such as the environment) that increase happiness and target policy accordingly. Social and cultural attitudes are important. One example is the number of hours spent working – Anglo-Saxon analysts tend to equate short hours with laziness.

What is the political balance required?

Audience comment

Do we need social sustainability in order to move forward on economic and environmental sustainability? Are governments likely to trade off more environmental regulation with less social intervention?

Panel response (led by Professor Soskice)

In the UK, change is easy to achieve so long as the middle classes benefit. Middle-class fears about security have led to the huge increase in imprisonment, and educational reform is designed to reassure middle-class voters about the quality of state schools. In Germany, however, the problem is that it is hard to achieve the wide social consensus needed for change. The UK has experienced strong economic growth, but (in broad terms) inequality has not decreased, while Denmark and the Netherlands combine a strong economy with only moderate inequality.

What leads to social inequality?

Audience comment

Social inequality used to be defined through broad issues of unequal access to health, education and so on. This approach seems outdated in the post-industrial society.

Panel comment (led by Professor Clasen)

Important factors that have affected this change include:

- the move from traditional full-time employment to non-typical employment patterns, with its implications for pension rights
- the reduction in collective bargaining (which now applies to a very small proportion of the workforce)
- high levels of long-term unemployment and inactivity, with large numbers of people outside the labour force
- ageing populations supported by smaller numbers of working people
- the impact of migration (especially in Germany, which tends to attract migrants with low levels of skills and education)
- the impact of selection in secondary schools – systems that stream large numbers of pupils into low-level vocational education fail to produce people with the skills needed for contemporary employment
- the influence of social and cultural institutions usually overlooked in this debate, such as the criminal justice system and marriage.



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creating sustainable growth in europe (csge)

is a major new policy research initiative from the Anglo-German Foundation. Designed to explore the complex problems confronting European economies today, csge will investigate how – if at all – we can increase economic growth without tipping the balance against social justice and the environment.

Four linked research programmes are taking up this challenge by pooling and comparing data, experience and new ideas from the UK and Germany, Europe's two biggest economies, and beyond. The initiative will culminate in 2009 with a series of conferences, publications and dissemination events.

For more information see www.agf.org.uk

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