



Europe 2008: The shape(s) of things to come

By Vernon J. Ellis

What will it be like to do business in Europe in 10 years?

Here are three possible scenarios, based on alternative views of the political, economic and social forces that are reshaping the Continent. Corporate strategists who begin anticipating changes now will be the best positioned to succeed.

Welcome to Europe, circa 2008. What sort of place is it? We have developed three different views of what Europe could be like in 10 years' time. These scenarios are not predictions of the future—rather they are different possible views of what might evolve, based on the application of a consistent combination of assumptions about relevant forces and trends. By looking at these alternative possibilities, companies can consider what they need to do now to be ready to cope with future developments, and to succeed, whatever happens.

Several themes are common to all three scenarios:

- New technologies and the rise of electronic commerce will increase market penetration, reduce the cost of customer contact and improve service.
- The quality of a company's staff is often the key differentiator, making it essential that people are treated as long-term assets.
- No effort should be spared to reduce

costs and increase productivity.

- Businesses must be alive to alliances that may enable them to exploit changes within and across industries and across political boundaries.

According to executives from some of Europe's leading companies, the main challenges business leaders will face over the next 10 years are achieving true customer focus, and having the right people, skills and culture. Industry relationships, delivery channels and operational flexibility will also be important, with costs and productivity an ever-present concern. These executives also told us that creating a new business culture and new skills, improving innovation and speed to market, and building new organizational models will be of critical importance.

But there was common agreement that the two most urgent initiatives should be to build a new customer/market approach and to optimize process productivity and efficiency.

In considering how to succeed within each European scenario, questions business leaders might consider include:

- How will the demands and values of my customers change?
- How will my markets extend and expand?
- How will my supply chain and value chain change?
- How will critical success factors differ?
- How will my management approach vary?
- What role should my business play in the wider community?

In thinking through these possible futures, companies can assess the challenges ahead and set their own priorities for action today.

COMPETITIVE EUROPE

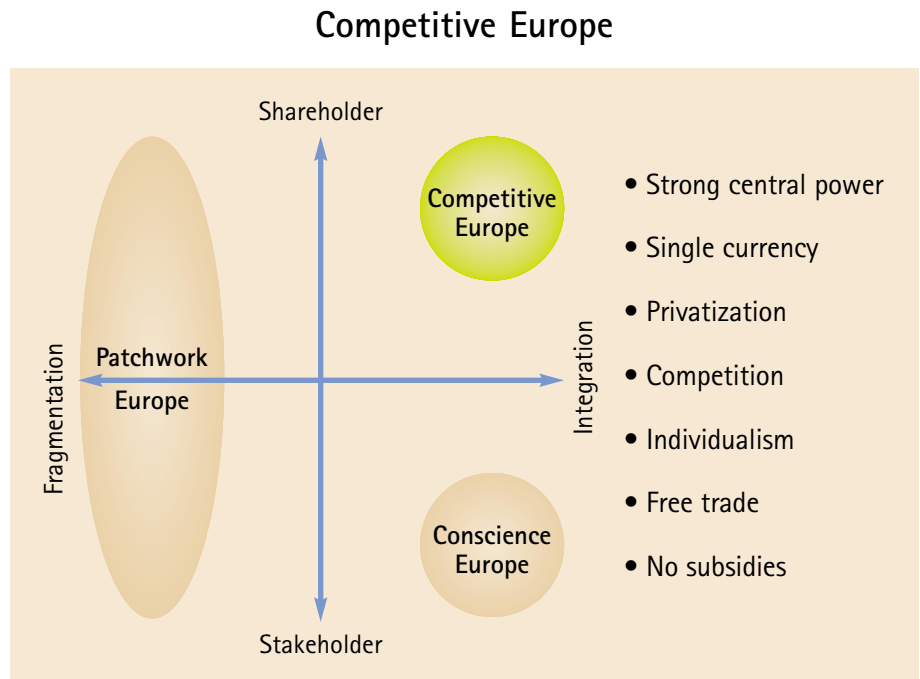
Europe is a good place to be in 2008—for those people who are members of the new European cosmopolitan class, well educated, well-off and well networked. But life is not so good for the poor, who are increasingly impover-

ished, lacking not just money but also access to ever more important information networks. There is a similar divide in terms of companies: The extremely competitive environment has created new business opportunities, but only for companies that are lean and nimble.

A strong euro—now adopted by all European Union member states after the nonparticipants were given an ultimatum to join European monetary union or to leave the EU—has acted as a particular spur for competition. The EU has gained new members, with countries like Poland and Hungary being admitted, and there have been further moves toward the completion of the single market. This has, in turn, provided a solid basis for European firms to compete more effectively in the global marketplace.

The days of big government are over, and power has gravitated toward EU institutions—not as the providers of services or subsidies but as the facilitators of an environment in which business can flourish. These institutions, now based in Berlin, have pushed much less of a social agenda in recent years, but where they do have authority they exercise this with great vigor. DG XXV, the powerful directorate general also known as the Free Enterprise Unit, has fought to place free market principles at the heart of the Union. The European Commission now has real teeth when it comes to competition policy. The thresholds for involvement of the commission have been lowered and its resources for investigating possible anticompetitive actions strengthened greatly.

Individualism and entrepreneurialism are now the dominant cultural forces throughout Europe. There has been a process of “competitive chaos,” with industry convergence and the reinven-



SOURCE: "EUROPE BEYOND THE MILLENNIUM," ACCENTURE

tion of markets being accompanied by the emergence of cross-sector players.

By 2005, privatization was virtually complete, and there is now intense competition between a small number of major companies in such formerly state-controlled sectors as utilities, telecommunications and transport. Mergers, acquisitions, joint ventures and alliances have led to massive economies of scale for multinationals—though hand in hand with this has come the growth of innovative small businesses in niche markets.

Companies must now have a commercial focus in everything they do. At the same time, companies are much more conscious of their relatively dominant role in society and the prominence—and exposure—this brings with it. They see it in their long-term interests to show responsibility toward the communities they are in, particularly over matters in which there is a high media risk, such as the environment. The first focus tends to be on action in the community, which has a fairly direct

payback to the companies themselves, such as vocational education—although as governments have reduced social security spending significantly, a number of major companies have seen it to be in their enlightened self-interest to plug some obvious gaps. The Unilever Business Institute in Amsterdam is perhaps the best example of where business has involved itself successfully in the European education system. It was the first of several private business universities across the Continent.

There have been moves toward an equity culture with a focus on return on capital. There is now a shorter-term approach aimed at achieving a fast payoff for shareholders. Pension funds in the EU have adopted strategies of holding minority shares in companies but have become the dominant investors overall. The increased pressure for swift returns has destabilized the traditional “insider” system of control, with financiers sitting on the board, and led to the breakup of long-run relationships.

The welfare state is greatly diminished, particularly with a major move away from state provision for both pensions and long-term care. Combined with the final round of privatizations, this has served to increase the size and volume of pension funds. The successful implementation of the single currency has dramatically increased the number of portfolios run on a pan-European basis. Indeed, the elimination of foreign exchange fluctuations, stable and low interest rates, lower transaction costs and transparent pricing have all combined to substantially reshape the financial services industry.

The global impact of Anglo-American capitalism has undermined Continental European stakeholding permanently, and as a result, there has been a dramatic shift in labor relations. There is now much greater uncertainty in terms of employment, with a greater use of short-term contracts and part-time and casual labor. Much of the national and EU employment regulation has been swept away on the theory that it was a burden on European firms that inhibited their ability to perform on the global stage.

The prevailing political philosophy is generally that everyone should be encouraged to work, with those social security payments that still exist tending to be in-work benefits. There are increasing numbers of both very high- and very low-paid employees. It is not only the latter group that has experienced a harder life in recent years: Senior managers must now live with uncertainty in extremely dynamic markets and constantly changing/reinvented supply chains.

A few years ago, immigration was actively encouraged in order to tackle the demographic problem of an aging population. This has proved to be successful in the short term, particu-

larly as a way of tackling the skills gap. However, a long-term solution still seems as far off as ever. In addition, there are now some danger signs, with increasing social conflict.

Given the nature of society, consumer demand is increasingly polarized between the high-income and the low-income markets; this means that firms need to be clear about which market segment they are targeting. Successful companies nowadays are ones that are flexible and customer-focused, ready to respond to demand with customized solutions, with firms catering to the needs of individual people across a whole range of markets rather than being constrained by traditional industry boundaries.

The enlargement of the EU has created growth in both the resources base and the consumer market. Many companies are now looking at investing and moving plants toward the Central and Eastern European countries and elsewhere to take advantage of natural resources and labor costs that are even lower than in the rest of the EU. The US utilities giants are beginning to align themselves with the Eastern European companies rather than those of Western Europe. This marks a change from the strategy of the mid-1990s, when consolidation in the Western European market was in vogue.

CONSCIENCE EUROPE

By 2008, the European Union has not only gained new members but also more power (although Europe now has slower, if more stable, economic growth). This influx of new members, and political changes within existing member states, meant that new cultures and philosophies developed. In particular, Anglo-American approaches to both the role of gov-



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EU institutions are more powerful than ever before. The union's decision-making processes have been streamlined, and this has paid off through greater efficiency in resolving tough issues like the Common Agricultural Policy and the so-called pensions time bomb, with a resultant increase in confidence in the EU. In recent years, we have seen more active government at the national level, although it is increasingly clear that it is in the institutions of the EU in Berlin where the real power lies.

There has continued to be a political realignment in many EU countries over the last few years, with perhaps the most popular philosophy at present being what has been termed "The Fourth Way," in which government increases its involvement in social welfare to levels not seen for 30 years and at the same time takes a vigorous approach to the scrutiny of firms and markets. Mergers and acquisitions now tend to be investigated thoroughly, not just in terms of their impact on competition, but also with regard to factors such as employment.

Welfare and tax regimes have been harmonized. It was successfully argued that the previous differences in these areas represented barriers to the successful completion of the single market, with some countries competing unfairly. Labor costs have risen substantially in recent years, with above-inflation increases in the European minimum wage now required by law in order to narrow the gap between rich and poor.

The European Commission is strongly involved in both transport and environmental issues, again on the grounds that these have an impact on the single market. Improved transport networks are seen as the way to make European economic integration a real-

ity, though these have required substantial subsidies.

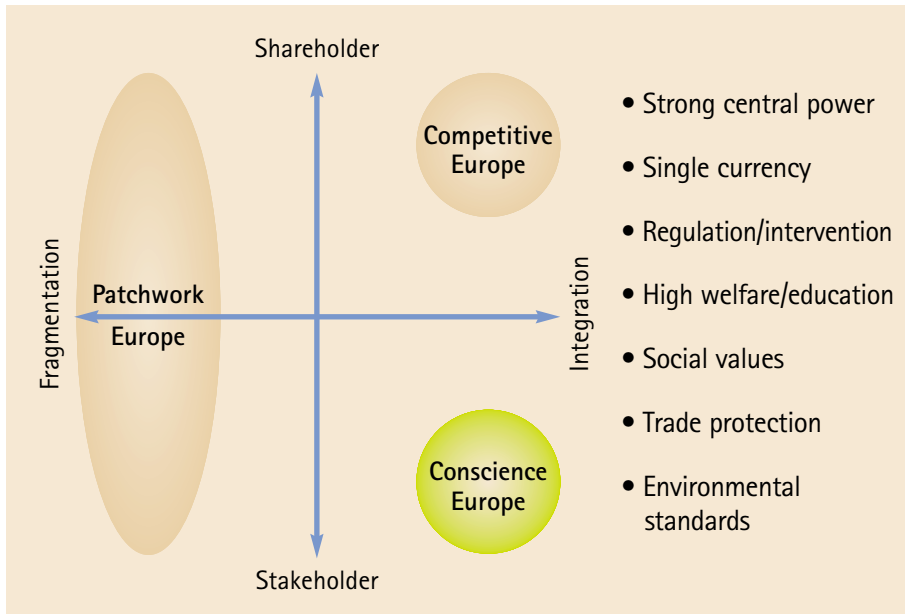
With regard to the environment, the commission argues that for too long companies have not been picking up the bill for the impact of their behavior, and it aims to levy stringent new taxes on polluters (though some industries have been excluded or given certain protection so that the additional costs do not render them so uncompetitive that jobs are lost). Businesses have had to learn to work inside an expanded but tightly regulated environment and to manage high social and labor costs.

These are boom times for EU policy experts, political lobbyists, strategists and lawyers—all are needed to ensure that firms understand and make the best use of EU legislation, structural funds and grants. Much of companies' and industries' interaction with the community is concentrated on lobbying the government to protect business interests. Business and society generally expect the government to take the leading role in meeting the needs of the wider community.

For their part, companies see a greater emphasis on partnerships and participation in government and EU-led initiatives. Given the high level of public expenditure, it is vital for individual companies that they get a share of the cake in areas such as infrastructure, training and research.

Some good news comes with the fact that this is a fairly stable environment in terms of public policy; business might not like the degree of regulation, but at least there is a high degree of certainty. This is a world in which entrepreneurship is not encouraged as strongly as it might be, but economic insecurity is not as prominent as it was in the past. There is less incentive for change, since there are few new entrants and the pace of both cross-

Conscience Europe



SOURCE: "EUROPE BEYOND THE MILLENNIUM," ACCENTURE

industry convergence and global competition has slowed dramatically.

Compared with 10 years ago, businesses now tend to take a more far-sighted view of supplier relationships, investment and other commercial decisions—"sustained and long-term investment for sustained and long-term return" is now the dominant philosophy. They treat employees as long-term assets, and match sensible recruitment programs with career planning. There is a strong emphasis on education and training, with the EU providing funds in order to improve Europe's skills base—although some business leaders have expressed concern that the link between such training and the needs of business is not always clear.

At the same time, companies tend to be wary of strategies that risk retaining too many staff in the event of an economic downturn, and hence investment tends to be capital-intensive where possible. Of course, investment in people rather than capital is often unavoidable, and some firms

have responded to the high social costs by trying to move parts of their operations outside Europe.

Income redistribution has led to the creation of a larger middle class. When combined with the impact of more rigid standards for many products and services, there has been a homogenization of product markets, resulting in a diminished range of choice. Regulation is at its toughest in sensitive areas such as health care, where a growing number of politicians are questioning the appropriateness of private-sector involvement.

The growth of the EU, in terms of both the number of members and degree of solidarity between them, has been accompanied by elements of a "Fortress Europe" approach, with restrictions on foreign competition, particularly when such competition is thought to have major employment implications. Again, this is justified in terms of the single market: It is said to be unfair that other countries can compete by having lower social standards.

This, in turn, causes problems with EU companies' access to overseas markets, as regulatory measures are put in place by way of retaliation. Many European businesses are still happily profiting from their protected home market, but there are signs that being shut off to an extent from markets outside Europe is resulting in less innovation. We could soon see a vicious circle, where the isolation of Europe leads to less innovation, and this, in turn, leads to even greater isolation because protectionism is seen as the only way to protect EU jobs.

"Fortress-busting" has become the name of the game for high-tech global businesses based outside the EU—and their consumers. Fed up with Europe's high prices and limited choice of goods, savvy consumers now surf the Internet for cheap, foreign-produced compact discs, films and other products, which can be downloaded without a customs official in sight.

PATCHWORK EUROPE

In the mid to late 1990s, pro-EU politicians accused their rivals of trying to create an unworkable "two-speed Europe." In 2008, many look back on these times fondly, for we now have something more like a 20-speed Europe.

The euro still exists, though it covers only a handful of countries. Every time Europe had economic problems, they were blamed on European monetary union, and the backlash in some countries was so strong that a number of the original participants withdrew and reestablished their own currencies. Others are soldiering on, but this is a confused and unstable environment for business.

All this has led to a far more insular and protectionist approach to trade. All EU member states still say that they are committed to the creation of

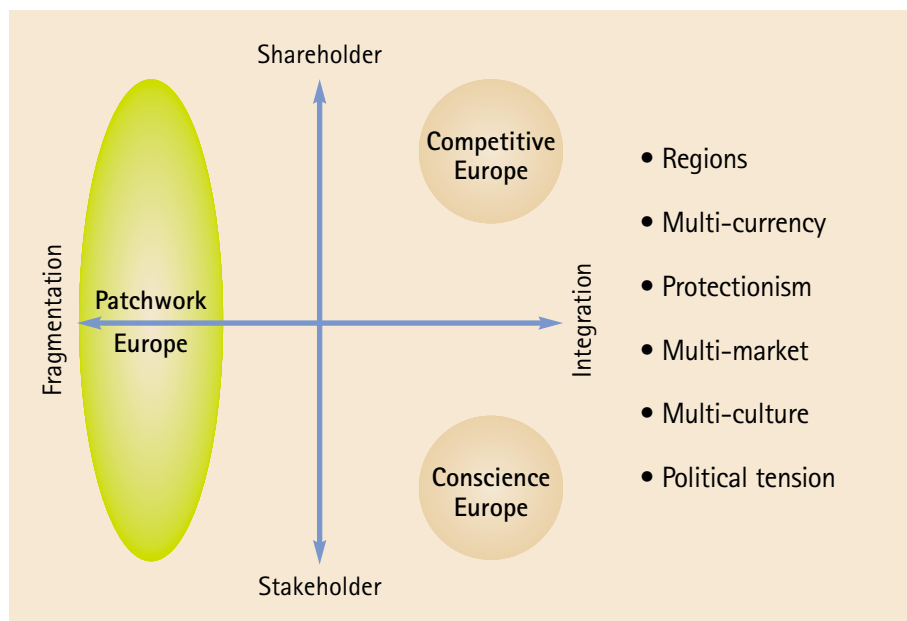
a truly effective single market. But the number of cases brought against member states by the European Commission for breaches in regulations governing issues such as state aid and public procurement, and for failure to implement new directives properly, has soared. There is an increasing amount of regulation at a European level but a declining level of national compliance.

There are de facto restrictions on the flow of labor and capital. This is a major problem for large businesses, which have always benefited from the advantage over smaller rivals of being able to transfer skills and knowledge effectively across borders. Although many industries are protected, there is little consolidation across Europe, so that opportunities exist in many areas for enterprising small businesses to exploit technologies such as the Internet to source, supply and sell across borders.

The accession of poorer countries that rely heavily on agriculture and old heavy industries, combined with the pensions time bomb, has put great stress on the finances of the European Union. The United Kingdom and Denmark are demanding that the EU not provide financial aid to those countries that have not already acted to scale down the state role in welfare provision, and other countries question why newer members should be given extra help to transform their economies at a time when longer-serving members are also facing economic difficulties.

The result is an absolute block on further social development of the union, and a reversion to something that has not been seen since the early Thatcher years in the United Kingdom: an evaluation of the impact of EU membership in terms of contributions paid in

Patchwork Europe



SOURCE: "EUROPE BEYOND THE MILLENNIUM," ACCENTURE

and grants paid out. No country has left the EU so far, but in the course of budget negotiations a couple have threatened to do so. All moves toward further widening have been frozen.

Creating effective relationships with government is hard for business, because power is located in so many different places. EU institutions have struggled to retain their authority since enlargement, as their mechanisms were designed for a smaller and less diverse membership, but they do still play an important role on some issues.

Recent years have seen the development of multilayered political structures with strong regional bodies, including not only the return of the city-state but also the creation of cross-border groupings. These bodies often have a different political perspective from that of relevant national governments—some pursue highly aggressive free market agendas, while others are much more interventionist; a third group seeks public-private

partnerships. This has led to some political tension and raises the sensitive issue for companies of how to establish good working relationships with one layer of government without offending another.

This complexity, in turn, affects the way firms relate to what in some parts of Europe are still referred to as "stakeholders." Firms need different identities in different places: The more sophisticated ones have become "multi-local," giving the impression in each area of a special commitment to that particular locality, with a series of different identities to fit in with the prevailing political and consumer culture.

Where the political culture favors unbridled capitalism, there is relatively muted involvement. But in other places there is much more high-profile sponsorship of community initiatives, with a focus on corporate responsibility and a sensitivity about issues such as the environment and executive pay.

Companies must manage at the most appropriate level. This will vary from region to region. Multinationals prosper, but only if they have political, legal and strategic competence in each marketplace. Human resources management and investment will require a longer-term strategy in some areas and a shorter-term approach in others.

But a broader view is still important. The winners will be those companies that can transcend political, cultural and geographic barriers, even while maintaining a range of appropriate identities for external audiences. Those firms that manage to transfer skills and knowledge across borders will have a major advantage over their competitors, both national and multinational.

However, many businesses' reaction to this complex picture has been to wonder whether they might be better off somewhere else. Central and Eastern European countries are now seen by many as prime candidates for investment, since they offer fewer operating restrictions and promise better returns. They have, in effect, become the engine of growth for Europe.

THE MOST LIKELY OUTCOME?

We make no attempt to predict which of these scenarios, if any, will actually exist in 10 years' time. But in light of the current sociopolitical environment, my personal view is that the most likely outcome lies somewhere in between Competitive Europe and Conscience Europe. Perhaps we might call this "Cooperative Europe."

The drive to meet the Maastricht convergence criteria has already forced Continental European governments to adopt many of the characteristics of the Competitive Europe scenario. They support the growth

of competitive economies and are developing a greater desire for labor market flexibility and reduced government spending.

At the same time, there is now a strong alliance of center-left social democrat governments across Europe that are strongly committed to promoting social cohesion. The current European political mainstream is keen to ensure proper support for security, well-being and education without returning to overly protectionist, interventionist social policies. This balanced approach might be termed "smart welfare."

Europe is currently experiencing a period of extreme discontinuity, and the outcome over the next 10 years matters very much to the success of businesses across the Continent. Trying to plan for the future by extrapolating from the past is a little like driving a car by looking in the rearview mirror: It tells you a lot about where you have come from but little about where you are going. In this time of unprecedented and accelerated change, we need to anticipate the unexpected and then plan to succeed, whatever the final outcome—perhaps even try to influence that outcome.

After all, this is not an academic exercise. A vibrant, successful and competitive Europe can bring real benefits to businesses and its citizens. We have everything to play for in shaping a successful and sustainable future. ■

This article is based on an Accenture study, "Europe Beyond the Millennium-Making Sense of Tomorrow."



Vernon Ellis is the Accenture managing director for Europe, the Middle East, Africa and India. Based in London, he has taken a particular interest in the firm's work with European stock exchanges. He has played a leading role in promoting the business perspective in debates about Economic and Monetary Union and the completion of the Single Market.