Don't Look to Europe, The U.S Needs Rehab Capitalism

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CNBC.com | 26 Jan 2010 | 07:20 AM ET

A year ago, the opinion makers at the annual World Economic Forum in Davos were so riveted by fears of global warming that they paid little attention to another threat. Not this year.

The western world appears to be in the grip of mechanisms squeezing much of the innovation out of its once-dynamic economies. Their financial sectors can ill-afford to pass up chances of big gains in order to finance the business sectors, especially start-ups, and their business heads can ill-afford to take their eyes off their earnings next quarter to think about long-term projects. The oft-predicted "decline of the West" may be real this time.

The signs include reduced levels of business investment and a slower trend growth rate of productivity and of real wages in large parts of the Western World; and, in some parts, a decade-long decline in job satisfaction, employee engagement and labor supply. No wonder President Barack Obama, on the eve of Martin Luther King Day, said that people are worried.

How to halt and reverse such a decline? There are few grand strategies still standing. The Old Left—socialism—officially expired with the collapse of the Berlin Wall. The Old Right—laissez-faire, or extremely free markets—was mortally wounded by the collapse of Bear Stearns and Lehman. (America's hard-right, tea-party types must forget about it.)

Now the "progressives" among U.S. economists propose a third way. This strategy would look to the government to offset the reduction in private business investment with increased public expenditure on capital and research, much as Keynes suggested during the 1930s Depression, and to reduce poverty with increased social insurance—more free medical care and housing.

Europe, they argue, adopted the strategy long ago with its huge public expenditure levels and expansive social insurance. And, they say, the outcome is that Europeans look as happy as Americans, their productivity and income levels are as high too and employment is lower only because leisure demand is higher. Europe even has more broadband. This demonstrates, they say, that the strategy works just fine. It delivers security, equality and prosperity too.

The truth is utterly different. To begin, Europe has been a distant second to the U.S. in dreaming up, developing, marketing and embracing new commercial products. The reason is not bad luck. Europe is lacking in economic dynamism—in systematically cultivating and facilitating innovation. This is evident by any measure:

- Venture capital investment in Europe is less than half the U.S. level.
- There are few start-ups in Europe—no **Microsoft**, **Netscape** or **Google** .
- In European countries the same old companies remain in the top 20 from decade to decade.

Some economic indicators convey the costs of this deficiency:

- Young people still leave Europe in droves to make their careers.
- Reported job satisfaction and employee engagement are far lower in France and Italy than in Canada and the U.S.
- Suicide rates are relatively high in some European countries.

The corporatist strategy of inserting the state in place of private initiative and creativity has never worked—from Mussolini onward.

In addition, social indicators point to moral failings in Europe.

- Except in the very homogeneous nations, we see stark failures to bring about economic inclusion—from Naples to Marseilles to Amsterdam.
- Kids growing up in slums have slim chances of having a good tertiary education and a rewarding career.
- The welfare state can be unjust.

So it makes no sense to regard the crisis of the American economic system as reason to glorify Europe's system, with its ghastly faults, or to see the latter system as a way out of decline. Sustained escape from decline will require a return to high dynamism and that will require bringing back old-fashioned banks that lend to business and old-fashioned companies that are forward-looking and courageous. A rehabilitated capitalism is the only vehicle that will get us there.

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