

# NEW DIMENSIONS OF ECONOMIC TRANSFORMATION – A EUROPEAN PERSPECTIVE

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## Abstract

*The 2020 Competitiveness Report published by the World Economic Forum brings up the notion of economic transformation of economies. The report identifies the main emerging priorities for countries to achieve economic transformation: moving towards full integration of social, environmental and institutional objectives into their economic systems over the next five years (approximately). At the same time, it is also trying to measure the degree of readiness of the countries to achieve such a transformation. The purpose of this endeavor is multifold: first, it maps priority areas against available data points in an effort to better define the actions and/or policies needed to "build better economies" that are productive, sustainable and inclusive; second, it provides a snapshot of the current situation in each country, assessing the extent to which countries today are on track to transform their economies, and third, it highlights where the main data gaps lie in policy evaluation and current national performance. In the light of these considerations, the purpose of this article is to highlight the European perspective on these new dimensions of economic transformation, on the inclusion of sustainable development objectives in the economic architecture of the European Union.*

**Keywords:** European Union, competitiveness, economic transformation, sustainable development, economic growth

**JEL classification:** F18, F43

## 1. Introduction

Sustainable economic growth was considered one of the fundamental objectives of the economic policy. Economic growth is not seen as an objective in itself, but only as a means to achieve the satisfaction of people's needs at the highest possible level. Recent developments reveal the fact that the emphasis seems to shift more and more towards the quality of life, economic growth being increasingly contested as the central objective of economic policy.

It is generally recognized that, with the globalisation of the economy, competitiveness has become one of the prime concerns of governments and firms.(OECD, 1996)

At the macroeconomic level, the competitiveness of a nation can be seen as the country's ability to achieve long-term economic growth in such a way that its economic structure adapts effectively to global economic evolution.

In 2001, within the World Economic Forum (WEF), it was proposed to calculate a competitiveness index, in order to determine the competitiveness of different states at the international level. After the analysis of the main elements to be evaluated, the Global Competitiveness Index (GCI) was established as a competitiveness evaluation indicator. GCI provides an integrative picture of the main factors that intervene in the formation of national competitiveness. These essential factors (pillars of competitiveness) depending on which the GCI is determined are grouped into three categories as follows: (1) basic requirements (institutions, infrastructure, macroeconomics, health services and education), (2) factors for increasing efficiency (higher education and human resources training, market efficiency, responsiveness to new technologies) and (3) innovation factors (quality of the business environment and innovation). (Ionci  et.al, 2008)

The *Global Competitiveness Report Special Edition 2020* series has, since its first edition, aimed to move focus beyond the growth-only paradigm and has been central at pointing out the need for public-private collaboration. The Global Competitiveness Index (GCI) contained in the report has continued to evolve along with the latest economic thinking,

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the needs of society and technological developments. The Global Competitiveness Index 4.0—launched in 2018—incorporates a wide-ranging focus on a broad range of factors of productivity. That year, we demonstrated that in the longer run there is a win-win-win between driving growth, creating better functioning societies and enacting measures to improve the environment.

The 2020 special edition of *The Global Competitiveness Report (GCR)* series comes out at a very difficult and uncertain historical moment. The outbreak of the COVID-19 pandemic has not only led to a global health crisis and deep economic recession—deeper than the downturn during the 2008–2009 financial crisis—but has also created a climate of profound uncertainty about the future outlook.

At this pivotal moment, there are growing calls for “building back better”. While the immediate priority is to respond to the health crisis, this moment in time also offers a unique opportunity to reflect on the fundamental drivers of growth and productivity that have degraded since the financial crisis. It is also a moment to determine how we may shape our economic systems in the future so that they are not just productive but also lead to environmental sustainability and shared prosperity.

The *Global Competitiveness Report* series has since its first edition aimed to prompt policy-makers beyond short term growth and to aim for long-run prosperity. The 2019 edition of the *Global Competitiveness Report* showed how declining trends in fundamental aspects of productivity have been masked by long-standing accommodative monetary policy but have remained bottlenecks for strengthening economic development.

This unusual moment calls for innovative and much-needed shifts in policy. Therefore, in 2020 the long-standing Global Competitiveness Index (GCI) rankings have been paused. Instead, this special edition is dedicated to elaborating on the priorities for recovery and revival, and considering the building blocks of a transformation towards new economic systems that combine “productivity”, “people” and “planet” targets. (WEF, 2020)

This special edition analyses historical trends on factors of competitiveness as well as the latest thinking on future priorities. It provides recommendations against three timelines: a) those priorities that emerge from the historical analysis before the health crisis; b) those priorities needed to restart the economy, beyond immediate responses to the COVID-19 crisis, while embedding people and planet into economic policies (revival over the next 1-2 years); and c) those priorities and policies needed to reboot economic systems in the longer run to achieve sustainable and inclusive prosperity in the future (transformation over the next 3-5 years). Recommendations and timeframes are grouped into four broad areas of action: 1) reviving and transforming the enabling environment, 2) reviving and transforming human capital, 3) reviving and transforming markets, and 4) reviving and transforming the innovation ecosystem. An initial assessment of countries on readiness for transformation is also provided that converts key priorities into quantitative measures for 37 economies. (WEF, 2020)

## **2. Emerging priorities for countries to achieve economic transformation**

The *Global Competitiveness Report* is structured around six sections. The first four sections analyse past and current trends by broad thematic areas that are the key building blocks of an economy: Enabling Environment, Human Capital, Markets, and Innovation Ecosystem. Within each of these thematic areas, priorities are presented for policy-makers to consider in order to develop productive, shared prosperity-enhancing and environmentally compatible economic systems. These priorities are organized into three timeframes: i) the past 12 years, assessing the evolution of key drivers of sustainable and inclusive productivity since the financial crisis, including the short-term shock impact of the COVID-19 crisis; ii) the next two years (revival), which looks at priorities to restart the economy while embedding criteria for longer-term productivity, inclusion and sustainability beyond immediate responses to the

COVID-19 crisis; iii) the next 3-5 years (transformation), which looks at the priorities for economic systems that fully integrate social and environmental targets into policy design. The fifth section of the report presents a first attempt to assess countries' readiness to achieve future transformation across all four thematic areas. The sixth section, through the lens of the Executive Opinion Survey, examines the disruptions caused by the crisis and identifies common elements of countries' resilience.

The key findings of the report are:

➤ Reviving and transforming the enabling environment

Before the COVID-19 crisis, a long-standing issue had been the ongoing and consistent erosion of institutions, as shown by declining or stalling checks and balances and transparency indicators. Against this backdrop, in the revival phase governments should prioritize improving long-term thinking capacity within governments and enhance mechanisms to deliver public services, including greater digitalization of public services. In the transformation phase, governments should work to ensure that public institutions embed strong governance principles and to regain public trust by serving their citizens. A second area of concern before the 2020 pandemic was high levels of debt in selected economies as well as widening inequalities. The emergency and stimulus measures have pushed already high public debt to unprecedented levels, while tax bases have continued eroding or shifting. To respond to these issues, in the revival phase, the priority should be on preparing support measures for highly indebted low-income countries and plan for future public debt deleveraging. In the longer run (transformation phase) countries should focus on shifting to more progressive taxation, rethinking how corporations, wealth and labour are taxed. This will require both national reforms and setting an international cooperative framework. Before the COVID-19 crisis, despite the significant expansions of ICT access, ICT availability and use remained far from universal. The COVID-19 crisis has accelerated digitalization in advanced economies and made catching up more difficult for countries or regions that were lagging before the crisis. To address this challenge, in the revival phase, countries should upgrade utilities and other infrastructure as well as closing the digital divide within and across countries for both firms and households. In the transformation phase, the priority should be on upgrading infrastructure to broaden access to electricity and ICT, while, at the same time, accelerating energy transition. (WEF,2020)

➤ Reviving and transforming human capital

For several years before the crisis, skills mismatches, talent shortages and increasing misalignment between incentives and rewards for workers had been flagged as problematic for advancing productivity, prosperity and inclusion. Because of the pandemic and subsequent acceleration of technology adoption, these challenges have become even more pronounced and compounded further by permanent and temporary losses of employment and income. To address these issues, countries should focus in the revival phase on gradually transitioning from furlough schemes to new labour market opportunities, scaling up reskilling and upskilling programmes and rethinking active labour market policies. In the transformation phase, leaders should work to update education curricula and expand investment in the skills needed for jobs in “markets of tomorrow”, and in parallel rethink labour laws for the new economy and use new talent management technologies to adapt to the new needs of the workforce. The COVID-19 crisis has highlighted a second issue: how healthcare systems' capacity has lagged behind increasing populations in the developing world and ageing populations in the developed world. To respond to this trend, countries should in the revival phase expand health system capacity to manage the dual burden of current pandemic and future healthcare needs. In the longer run (transformation) there should be an effort to expand eldercare, childcare and healthcare infrastructure and innovation. (WEF,2020)

➤ Reviving and transforming markets

Over the past decade, while financial systems have become sounder compared to the pre-financial crisis situation, they continued to display some fragility, including increased corporate debt risks and liquidity mismatches. In addition, access to finance, despite efforts to increase inclusion in recent years (including through fintech applications), is not sufficiently widespread. Against this backdrop, countries should in the revival phase prioritize reinforcing financial markets stability, while starting to introduce financial incentives for companies to engage in sustainable and inclusive investments. In the transformation phase, the attention should shift to create incentives to direct financial resources towards long-term investments, strengthening stability while continuing to expand inclusion. Pre-crisis, there was increasing market concentration, with large productivity and profitability gaps between the top companies in each sector and all others; and the fallout from the pandemic and associated recession is likely to exacerbate these trends. To address this issue, countries should in the revival phase strike a balance between continuing measures to support firms and prevent excessive industry consolidation with sufficient flexibility to avoid keeping “zombie-firms” in the system. In the transformation phase, countries should rethink competition and anti-trust frameworks needed in the Fourth Industrial Revolution, ensuring market access, both locally and internationally. As a complementary policy, countries should facilitate the creation of “markets of tomorrow”, especially in areas that require public-private collaboration. A third trend that has emerged in this area is the ongoing reduction on trade openness and the international movement of people, now vastly stalled due to the pandemic. In both the revival and transformation phases, countries should lay the foundations for better balancing the international movement of goods and people with local prosperity and strategic local resilience in supply chains. (WEF,2020)

➤ Reviving and transforming the innovation ecosystem

In this area, a paradox had recently emerged: a positive evolution of entrepreneurial culture in the past decade, but the creation of new firms and breakthrough technologies had stalled. Technology has lagged especially in the capacity to delivering solutions to energy consumption, emissions and meeting the demand for inclusive social services. To manage these complexities, countries should in the revival phase expand public investments in R&D, incentivize venture capital and R&D in private sector, and promote the diffusion of existing technologies that support the creation of new firms and employment in “markets of tomorrow”. In the longer run (transformation) countries should create incentives that favour patient investments in research, innovation and invention, support the creation of new “markets of tomorrow” and incentivize firms to embrace diversity, equity and inclusion to enhance creativity. (WEF,2020)

**Table 1. Priorities identified in the recovery and transformation phase**

	<b>Trends and Crisis Impact</b> <i>From the financial crisis to the pandemic crisis</i>	<b>Revival</b> <i>Priorities for the next 1-2 years</i>	<b>Transformation</b> <i>Priorities for the next 3-5 years</i>
Reviving and transforming the enabling environment	There has been a consistent erosion of institutions across regions, including weaker checks and balances and less transparency.	Improve the long-term thinking capacity within governments and mechanisms to deliver public services and support policy interventions digitally.	Ensure public institutions embed strong governance principles and along-term vision and build trust by serving their citizens

	<b>Trends and Crisis Impact</b> <i>From the financial crisis to the pandemic crisis</i>	<b>Revival</b> <i>Priorities for the next 1-2 years</i>	<b>Transformation</b> <i>Priorities for the next 3-5 years</i>
	ICT access and use have been improving globally but remain far from universal, and the COVID-19 crisis has made catching up more difficult for developing economies while deepening advanced economies' digitalization.	Upgrade utilities and other infrastructure.  Prioritize closing the digital divide within and across countries for both firms and households	Upgrade infrastructure to accelerate the energy transition and broaden access to electricity and ICT.
	Emergency and stimulus measures have pushed already high public debt to unprecedented levels, against a backdrop of shifting tax bases.	Prepare support measures for highly-indebted, low-income countries and plan for future public debt deleveraging.	Shift to more progressive taxation, rethinking how corporations, wealth and labour are taxed, nationally and in an international cooperative framework.
Reviving and transforming human capital	Talent shortages have become more pronounced, underpinned by outdated education systems. There is a particular shortfall in digital skills and other skills of the new economy as technology disrupts labour markets.	Scale up reskilling and upskilling in emerging skills, combined with active labour market policies.	Update education curricula and expand investment in the skills needed for jobs and "markets of tomorrow".
	There are misaligned incentives and rewards for workers.	Manage a gradual transition from furlough schemes to new labour market opportunities.	Rethink labour laws and social protection for the new economy and the new needs of the workforce.
	Health services, infrastructure and talent have lagged behind two dominant demographic trends: increasing population in the developing world and ageing populations in the developed world.	Expand health system capacity to manage the dual burden of current pandemic and future healthcare needs.	Expand eldercare, childcare and healthcare infrastructure, access and innovation for the benefit of people and the economy.
Reviving and transforming markets	Financial systems after the 2007–2008 crisis have become sounder but continue to have some sources of fragility, including increased corporate debt risks and liquidity mismatches, and are not sufficiently inclusive.	Ensure stable financial markets, a sound financial system and expand access and inclusion.  Create financial incentives for companies to engage in sustainable and inclusive practices and investments.	Increase incentives to direct financial resources towards long-term investments, strengthen stability and expand inclusion.

	<b>Trends and Crisis Impact</b> <i>From the financial crisis to the pandemic crisis</i>	<b>Revival</b> <i>Priorities for the next 1-2 years</i>	<b>Transformation</b> <i>Priorities for the next 3-5 years</i>
	Market concentration has been on an increasing trend in advanced economies, with large productivity and profitability gaps between the top companies and all others in each sector.  Trade openness and the international movement of people have been on a declining trend since the financial crisis.	Lay the foundations for better balancing the international movement of goods and people with local prosperity and strategic local resilience in supply chains.	Rethink competition and anti-trust frameworks needed in the Fourth Industrial Revolution, ensuring market access, both locally and internationally.  Facilitate the creation of “markets of tomorrow”, especially in areas that require public-private collaboration.
Reviving and transforming the innovation ecosystem	Entrepreneurial culture has strengthened in the past decade but has not resulted fully in the creation of new firms.  There is a lack of sustained creation of breakthrough technologies and, where there has been innovation, it has not been widely successful at delivering solutions to increasing energy consumption, managing emissions and meeting the demand for inclusive social services.	Expand public investments in R&D, and incentivize venture capital, R&D in private sector and the diffusion of existing technologies that support the creation of new firms and employment in "markets of tomorrow".	Incentivize and expand patient investments in research, innovation and invention that can create new “markets of tomorrow”.  Incentivize firms to embrace diversity, equity and inclusion to enhance creativity.

Source: (WEF, 2020)

### 3. Assessing the degree of readiness of countries for economic transformation

For a country, achieving economic transformation means moving towards a full integration of social, environmental and institutional objectives into economic systems. Measuring the degree of readiness of countries to achieve such a transformation involves identifying a preliminary set of concepts to break down the 11 emergent priorities identified by the authors of the report, then the indicators compared to them were identified, data were collected and the results were calculated for the 37 economies analyzed.

The 11 emerging priorities identified are:

1. Ensure public institutions embed strong governance principles and a long-term vision and build trust by serving their citizens
2. Upgrade infrastructure to accelerate the energy transition and broaden access to electricity and ICT
3. Shift to more progressive taxation, rethinking how corporations, wealth and labour are taxed, nationally and in an international cooperative framework
4. Update education curricula and expand investment in the skills needed for the jobs and “markets of tomorrow”
5. Rethink labour laws and social protection for the new economy and the new needs of the workforce

6. Expand eldercare, childcare and healthcare infrastructure, access and innovation for the benefit of people and the economy
7. Increase incentives to direct financial resources towards long-term investments, strengthen stability and expand inclusion
8. Rethink competition and anti-trust frameworks needed in the Fourth Industrial Revolution, ensuring market access, both locally and internationally
9. Facilitate the creation of “markets of tomorrow”, especially in areas that require public-private collaboration
10. Incentivize and expand patient investments in research, innovation and invention that can create new “markets of tomorrow”
11. Incentivize firms to embrace diversity, equity and inclusion to enhance creativity.

The aim of this exercise is three-fold. First, it maps the areas of priority against available data points in an effort to better define the actions and/or policies needed to “build back better” economies that are productive, sustainable and inclusive. Second, it provides a snapshot of the current situation in each country, assessing the extent to which countries today are on the way towards transforming their economies. Third, it highlights where the key data gaps lie in assessing current national policies and performance. (WEF,2020)

The authors of the report point out the following aspects regarding the economic transformation:(WEF, 2020)

✓ Future-oriented institutions will not only need to be transparent and efficient; they must also evolve towards yielding more equitable outcomes and enhancing citizens’ trust in them. Governments will also be increasingly called upon to communicate clearly a longer-term vision, anticipating the evolution of trends, and build structures that will allow for agile responses to future shocks and rapid technological change.

✓ The transition to a greener and more inclusive economy will have to be underpinned by significant investments in infrastructure, including an expansion of digital networks. Greening the economy will require upgrading energy infrastructure and transport networks in addition to commitments from both public and private sectors to extend and respect multilateral agreements on environmental protection.

✓ When it comes to updating tax structures, the key tension to resolve will be between ensuring a fair transition and setting the right incentives for technology adoption and innovation. An updated tax architecture will require policy-makers to rethink relative burdens across income, wealth and corporate taxes in light of these trade-offs.

✓ Reskilling, upskilling and education curricula updates are central to prepare workers and achieve inclusive prosperity. Participation in formal education is no longer sufficient to provide employment opportunities and build human capital. Instead, education systems should be upgraded to provide digital skills and critical thinking skills through schools and universities, as well as ongoing learning and skilling through public and private life-long learning programmes.

✓ One important component of policies to curb inequality and manage the technology- and recession-driven shifts in the workforce is adequate and agile social safety nets. Future-looking approaches should better integrate income support with adaptation of labour laws and expand the social protection floor, including easing access to education, training and health to support the full development of citizens’ human capital. This approach should succeed in protecting and rewarding workers rather than jobs—and deploying technology to facilitate the shifts for workers is crucial.

✓ Universal access to eldercare, childcare and healthcare is a fundamental factor for building fairer societies while empowering human capital. A combination of adopting new technology and expanding investments in this domain could help to address this priority.

✓ A thriving financial sector should channel resources towards long-term investments in the real economy rather than maximize short-term profits or support financial markets. The growing importance of ESG (environmental, social and governance) standards for investing bodes well for the capacity of the financial system to move in this direction.

✓ While market concentration has increased in the past decade, modern policies to restore competition will need to consider new drivers of market concentration (e.g. intangible assets, digital platforms) and update their toolkit accordingly.

✓ Trade openness also contributes to the creation of more competitive markets; future policies should innovate on how to maintain the benefits of international trade while limiting internal divides between regions where world-class companies are located and support regions and sections of the population that lose out from globalization.

✓ Future-oriented policies will need to combine push-and-pull strategies, including incentivizing demand and investments in R&D towards the production of more sustainable and inclusive goods, services and technologies. At the same time, bottlenecks in the diffusion of breakthrough innovations from a niche frontier to the rest of the economy should also be removed.

✓ Diversity, equity and inclusion must be an integral part of an innovation-driven strategy for economic transformation. Companies must fully leverage the creative potential of different segments of the population and access to the opportunities generated through innovation should be expanded via, for instance, facilitating inclusion in ownership of new innovative businesses, employment in research roles, and career progression in growing markets.

The main contribution of this exercise is to provide an assessment of countries' readiness on each of the 11 priorities for transformation.

The key take-aways of this exercise are that organizations such as the World Economic Forum must better measure the capacity of countries to transform and expand data availability, and that no country is yet ready to transform its economy. However, among the existing policies, and based on available statistics, the 'Nordic model' is the most promising in leading economic systems towards greater sustainability and shared prosperity. These countries (e.g. Finland, Denmark, Sweden) are among the best-prepared on most of the 11 priorities identified by this framework and are, consequently, among those that are most ready for an economic transformation.

Denmark and Finland appear among the top 3 score on the 11 categories of transformation four times, while Sweden appears three times. Across all categories however, most economies have a long way to go to attain "maximum" scores and measurement concepts and data availability must be expanded to provide a more detailed picture of transformation readiness.

#### **4. Conclusion**

The deep economic recession triggered by COVID-19 continues to have profound economic and social consequences. Since the outbreak of the pandemic, unemployment rates have risen rapidly in most developing and advanced economies, and poverty rates have begun to rise again, reversing the gains made in recent decades. The crisis has also exposed the inadequacy of existing infrastructure and policies, from social protection systems to healthcare. The global economic outlook is highly dependent on both the evolution of the pandemic and the effectiveness of governments' recovery strategies. In this unique context, the authors of the Global Competitiveness Report look at how countries can expand their focus beyond a return to growth and how to "build back better". The report looks at priorities for savings in three time frames: those of the past decade, as revealed by time series data on competitiveness factors, those that are essential for economic recovery, as highlighted by the crisis, and those that could contribute to mainstreaming a transformation that could lead to better outcomes for productivity, shared prosperity and sustainability. The road to economic recovery will be long, asymmetric and asynchronous across economies and can be proactively shaped and managed for optimal outcomes for productivity, people and the planet.



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