

HIDDEN TREASURES

Europe's structural advantages in stimulating innovation

Dr Donald Kalff, Berlin, November 28, 2019



The Hidden Treasures Program

The book

Mapping Europe's sources of competitive advantage
in doing business

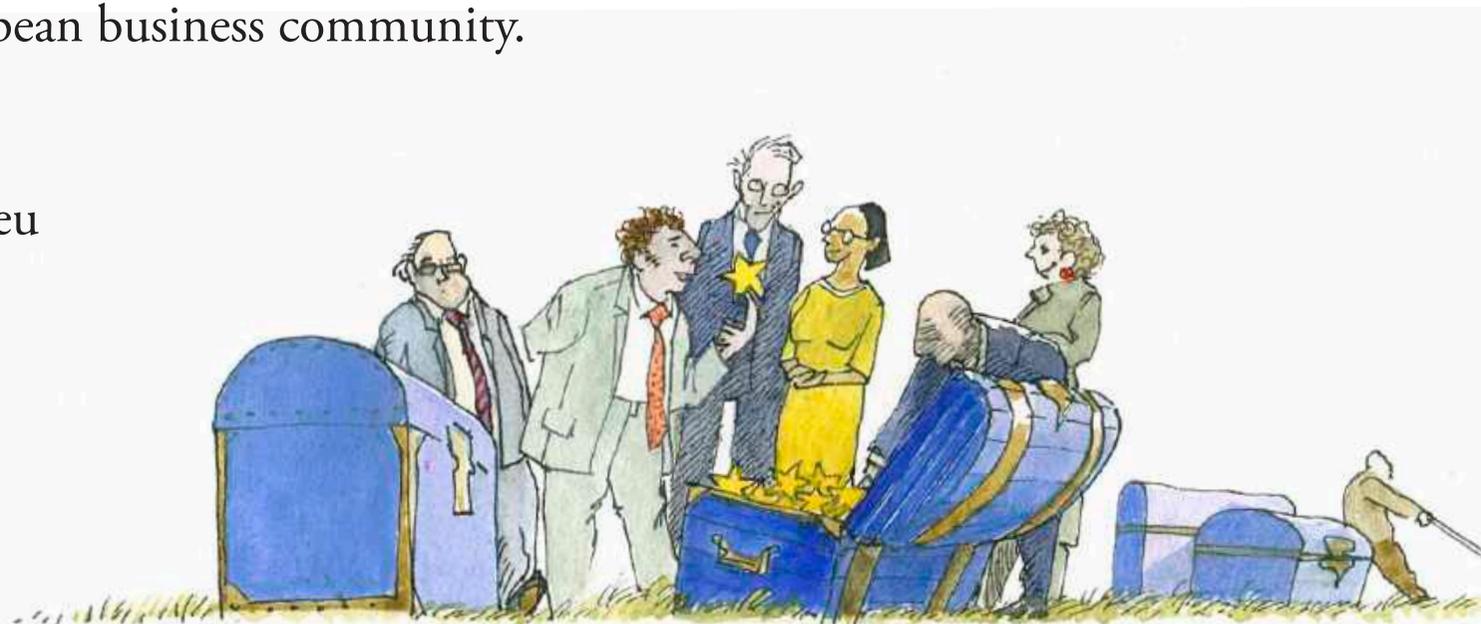
by Donald Kalff and Andrea Renda

The program

A three-year effort to bring 40 recommendations to life and to draw attention to comparable initiatives of third parties in cooperation with the European Commission, the European Parliament and the European business community.

The website

hiddentreasuresprogram.eu



Hidden Treasures and Innovation

- * **Contract formation and dispute settlement**
- * The position of SME's vis-a-vis large companies
- * The European patent system
- * A wide range of enterprise models
- * **The European Enterprise**



Contract formation and dispute settlement

EU26

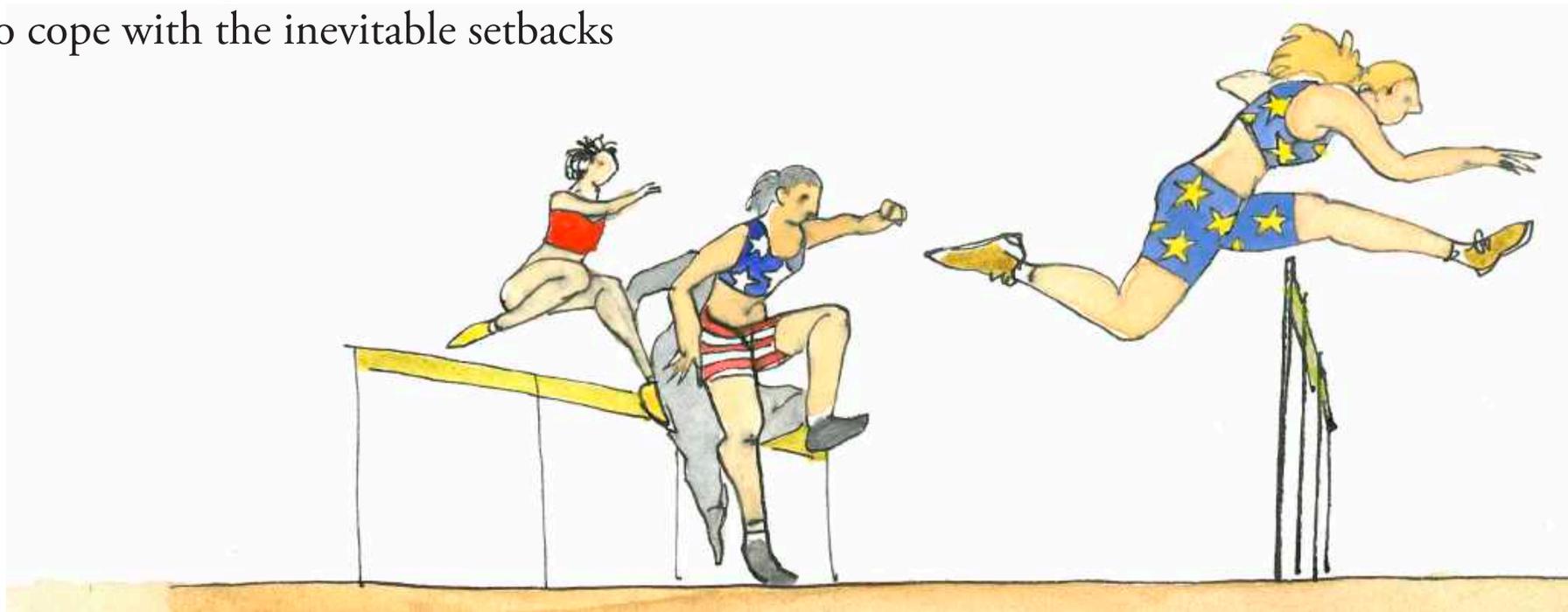
- * Good faith obligation enshrined in law
- * Reasonableness and fairness as guiding principles
- * Precontractual and post contractual obligations
- * "Culpa in contrahendo"

US, UK, Ireland

- * Good faith obligation at best part of existing contracts
- * The principle of private autonomy
- * The freedom to contract
- * The prosecution of self interest

EU 26 more competitive

- * Reduction of value destruction caused by last minute withdrawals
- * Innovation is inherently unpredictable, hence the need for framework agreements
- * Innovation increasingly depends on cooperation of multiple partners
- * Facilitation of the outsourcing of innovation by large companies
- * Early commitment helps to build the trust required to cope with the inevitable setbacks



Strengthen what is already strong

- * Promote the use of civil law
- * Invest in the civil courts
- * Establish specialized courts in IT, AI, Biotech and Nanotechnology
- * Enhance the quality of legal support
- * Improve access to the court system for SME's
- * Invest in decentralized and EU low entree conflict resolution mechanisms



The European Enterprise

Lack of economic growth has not only macro- but also micro-economic causes

Value destruction and lack of value creation by large listed companies are not caused by adverse market conditions or geopolitical turmoil, but by a number of fundamental choices that shape corporate governance and management





Poor performance of large listed companies

- * Growth of investment lackluster
- * Return on investment shrinking
- * Export growth decreasing
- * Productivity growth sharply declining
- * Share of new products in total revenues stagnating
- * Scandals revealing structural shortcomings in governance and management

... whilst historically high margin and profit growth is not sustainable

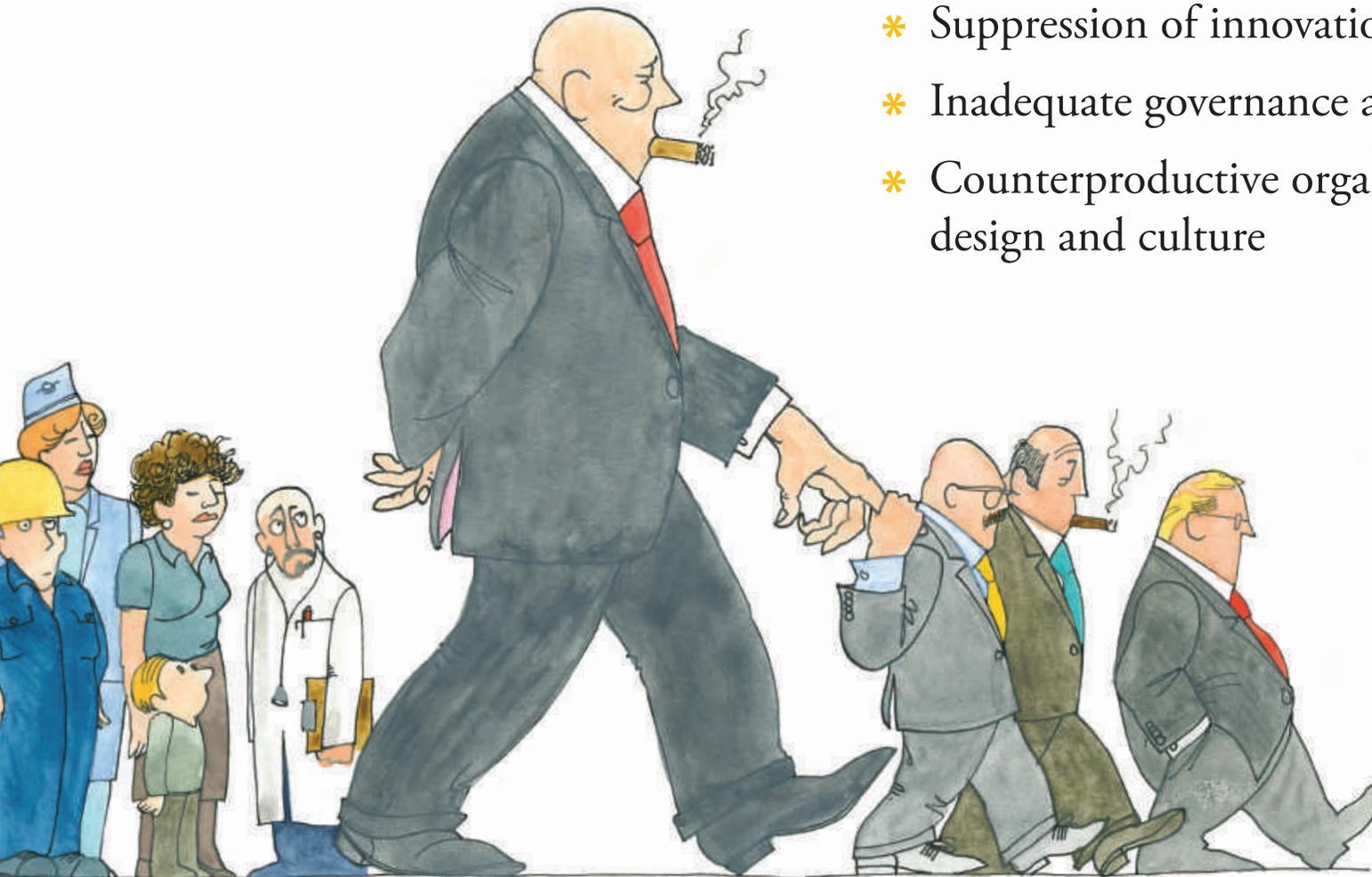


Under extraordinarily favorable circumstances

- * ICT revolution served outsourcing, market access and marketing
- * Increased pricing power due to industry consolidation
- * A low and decreasing effective tax rate
- * Unprecedented low inflation and lowest cost of capital ever
- * Until recently, a de facto freezing of wages
- * Highly effective lobbying in defense of established (market) positions
- * Large incentives provided by competing cities, regions and countries

Flaws in the shareholder model

- * Serves financial markets, not the economy
- * Emphasis is on control and transfer of risk
- * Artificial investment hurdles
- * Harmful commercial doctrines
- * Suppression of innovation
- * Inadequate governance and management
- * Counterproductive organizational design and culture



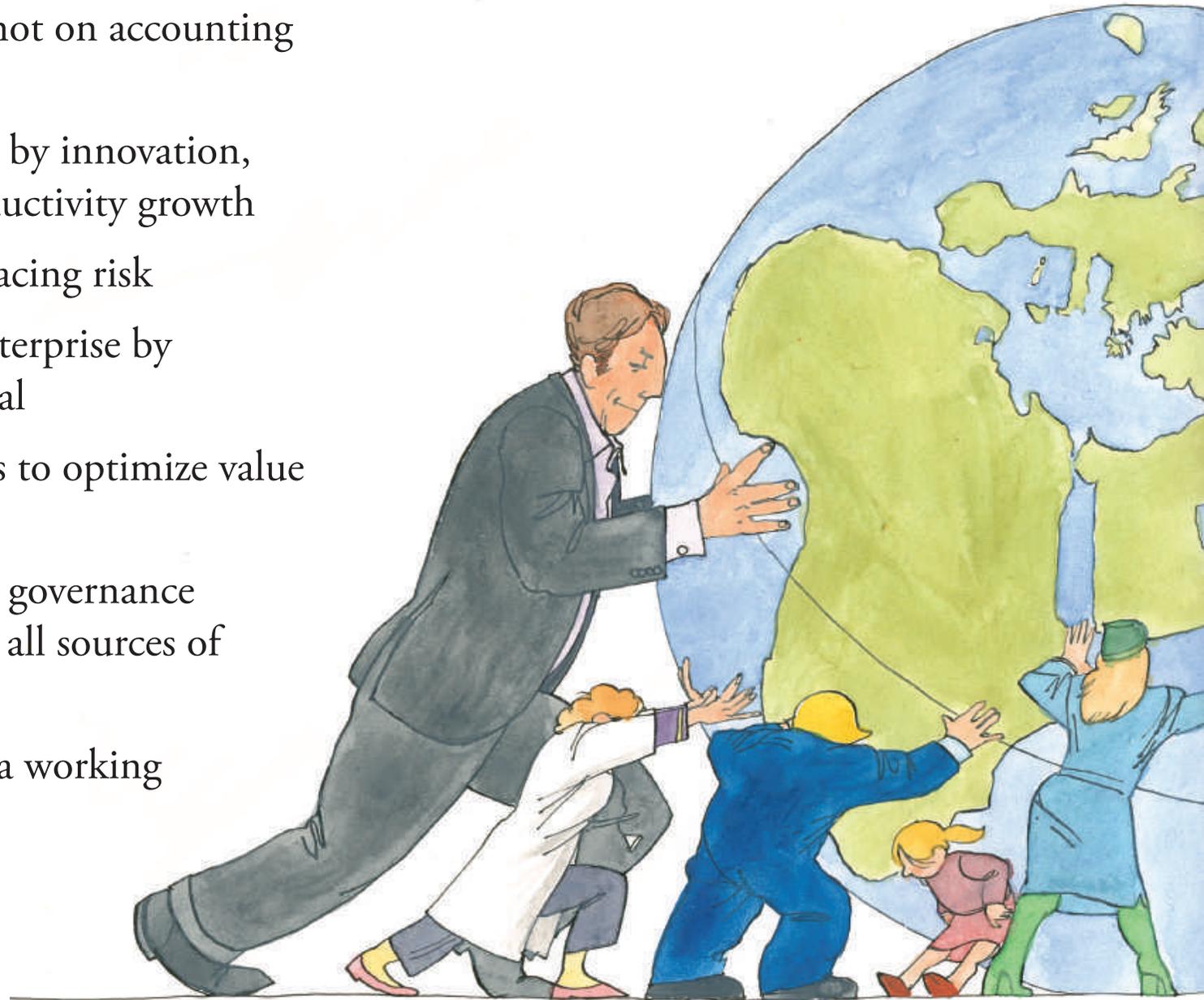


Flaws in the stakeholder model

- * Serving special interests at the expense of the development of the enterprise
- * Steering clear of risk, avoiding and suppressing conflicts
- * Stakeholders exercise power without responsibility and accountability
- * Stakeholders defend established positions and depend on short-term successes
- * Stakeholders constrain innovation
- * Inadequate governance and management
- * Counterproductive organizational design and culture

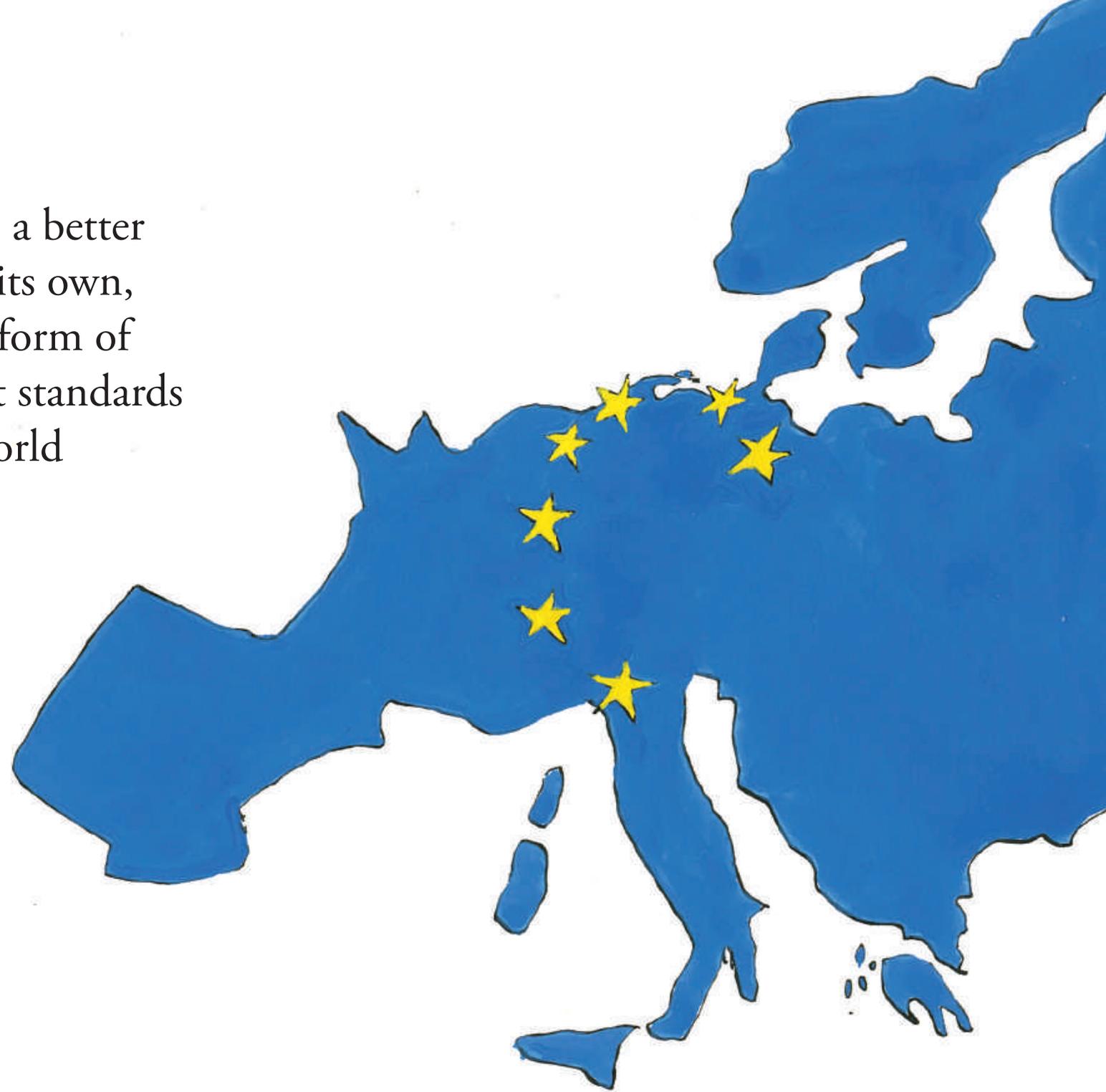
The European Enterprise model

- * Operating license provided by society at large
- * Focus on economic profit, not on accounting profit
- * Creation of economic value by innovation, by investments and by productivity growth
- * Facing the future and embracing risk
- * Retaining control of the Enterprise by diversifying sources of capital
- * Engagement in partnerships to optimize value creation
- * Entrepreneurship built into governance and management to exploit all sources of economic value
- * The enterprise functions as a working community



	Shareholder Model	Stakeholder Model	European Model
Source of legitimacy	Shareholder	Stakeholder	Society
Worldview	Financial	Political	Economic
Attitude to risk	Transfer and control	Steering clear	Facing uncertainty
Modus operandi	Analytical	Probing	Holistic
Overriding objective	Shareholder ROI	Eclectic	Creation of economic value
Steering variable	Profit per share	Multiple	Free cash flow
Principle source of finance	Stock market	Banks	Diverse
Leadership	Individual	Committee	Dispersed
Culture	Competition among individuals	Competition between units	Cooperation
Management	By rule	By principle derived rules	By principle
Decision making	Procedure driven	'Horses for courses'	Quality driven
Enforcement	Exercise of power	Building support	Corporate interest leading
Control	Command and incentives	Formal commitments	Professional standards

Europe was never in a better position to develop its own, highly competitive, form of capitalism and to set standards for the rest of the world



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