UDC: 338:339.137.2(4-672EU)
JEL: O24, F10 COBISS.SR-ID 211780364
ORIGINAL SCIENTIFIC PAPER

# Competitiveness of the European Union: Pre-crisis Trends and Impact of the Financial Crisis

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***ABSTRACT*** *– This paper has the aim to point out the risks of reducing the EU competitiveness by analyzing the indicators of price and cost competitiveness, as well as the structural and technological aspects of competitiveness. The influence of the world crisis on the competitiveness and export performances of the EU is in the focus in order to show at what extent the global downturn may have aggravated previously existing needs for readjustment of the functioning of the Union. Not only that the crisis showed that the problems in the Union were not created recently, but also it demanded urgent needs of new improved policy in order to regain the competitiveness strength and performances.*

*The reformulated strategy needs to be based on openness and innovation, with investment in research and development. Long-term expectations are to be made comprehensive structural changes in order to overcome structural differences between individual Member States and to increase the overall competitiveness. Additionally, trade barriers are needed between individual Member States to be removed and higher individual and aggregate rates of economic growth are to be achieved. It is clear that the effects of deep integration of the EU has not yet been achieved, and expected benefits may not be realized, if internal and external balance of the Union is not maintained.*

***KEY WORDS****: competitiveness, trade, exchange rate, technology, productivity*

## Introduction

Over the past two decades, European Union (EU) managed to hold its position on the world market, competing with the USA and Japan, and as well as with new rivals such as China and India. But even before the crisis, the productivity growth started slowing down and the EU faced with the serious challenges of losing world market positions due to the loss of competitiveness.

Under the term ''competitiveness'' in the literature can be found many different definitions. Generally, an economy is competitive if it does things that are likely to encourage economic growth. The simple measure of economic growth is the value of the

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gross domestic product (GDP). But, if a country is increasing its GDP that would not mean that the country's competitiveness has improved. For instance, if the growth is based on natural resources and their favorable price developments, the GDP will grow (GDP= quantity multiplied by prices), but the economy will not have significant improvements in the competitiveness. In case, the reason for the dynamics and the quality of economic growth is determined from the level of labor productivity, then we can make difference. In the macro economy it is widely accepted that the difference in labor productivity is the reason for the great differences in the level of economic growth in the countries in the world economy (Mankiw, 2010).

Krugman (1996) has also declared that the real essence of competitiveness is reflected in the productivity. Still, many economists believe that not only the quantity of economic production is important, but also the quality of living of the people (Aiginger, 2004). That would mean, greater opportunities for education, healthy life, rich cultural life etc. That can be measured by the second indicator of economic growth, GDP per capita. Higher the GDP per capital means higher living standards of the population. Still, GDP per capita does not take into account the country's ability to distribute the gained wealth in a fair manner (it is calculated on average level). Another weakness is that we can get wrong conclusion. For example if we have the same value of the GDP, but decreasing growth rates of population, we will get higher GDP per capita.

Some authors (Haiman & Altena, 2007) find the linkages between competitiveness and trade (traditional theories). Popular discussion often views 'competitiveness' as a way to narrow the current account deficit of the balance of payments. That can be measured by the growth of the export of the market share (participation of the total value of the export in the total world export). The essence of this theory is compounded by openness to trade tending to be associated with openness to ideas. Especially for small economies, openness to trade should boost economic growth by increasing domestic competitive pressures (from imports) and allowing domestic producers access to wider markets and so economies of scale (from exports). Still these theories do not take into account the quality of the product or the service or the branding of the products. On long run, non pricing factors (structural and technological aspects) such as: research and development, regulatory regime and other have significant influence on the competitiveness of the products and of the economy.

Finally, if we summarized all the above mentioned views, the competitiveness of one country can be defined as ability of the country to compete on the world market, with final goal to increase the wealth of the country and the living standards (Ottaviano at al., 2009).

The definition according to the traditional theories will be applied in the context of the paper. In the first section, the trends in the world trade and EU trade are analyzed, from the creation of the European Economic Community to 2010. In the second section the discussions about the indicators of competitiveness will take place. The approach towards the EU competitiveness will be analyzed according to the traditional approaches that consider the successful export performance – either in terms of export growth or export market share and by the standard indicators of cost and price competitiveness. To determine the price competitiveness, the real effective exchange rate is used. Cost competitiveness is analyses by the ULC (unit labor costs) in manufacturing sector and consumer price deflator in order to see the trend of the movement of the real effective exchange rate. Also, additional data from

the Global Competitiveness Report (World Economic Forum, 2013) and of Europe 2020 Strategy will be integrated in the paper in order to give multi-dimensional concept of competitiveness. In order to overcome the flaws of the traditional theories in the third section, technological aspects and other aspects of the non-price competitiveness of the EU will be elaborated.

This paper has the aim to point out the risks of lowering the EU competitiveness. The influence of the world crisis on the competitiveness and export performances of the EU is in the focus in order to show at what extent the global downturn may have aggravated previously existing needs for readjustment of the functioning of the Union. Not only that the crisis show that the problems in the EU were not created recently, but also ask for urgent need of new improved policy in order to regain the competitiveness strength and performances.

The methodology of this research is based on quantitative analysis. It will be presented in a form of time series analysis for the case of EU, concerning the period 1958-2012, and for the indicators of competitiveness 2000-2012 in order to point out the dependence among observations at different points in time. Core suppliers of the needed data will be the Euro stat, International Monetary Fund and UN Comtrade databases.

The expected outcome of the research is to summaries the main reasons that contribute to loss of the world trade positions of the EU which will lead to conclusions about the future prospects of the EU and need for high productive strategy.

## Trends in the world trade and trade of the EU

Global external imbalances widened persistently over the last several years. International trade flows contracted sharply in the fourth quarter of 2008 and first quarter of 2009 mainly due to the decline in the economic activity and aggregate demand, which was result of the beginning of the world economic crisis, the percentage decline of the world trade in 2009 compared to 2008 was 22.73% (table 1).

*Table 1. Annual growing rates of the world trade by region and selected economies (%)*

| | 2006 | 2007 | 2008 | 2009 | 2010 | 2011 | 2012 |
|---|---|---|---|---|---|---|---|
| World | 15,38% | 15,24% | 15,45% | -22,73% | 21,79% | 19,54% | 0,30% |
| North America | 11,90% | 7,97% | 8,83% | -23,56% | 22,97% | 15,62% | 3,54% |
| South and Central America | 21,07% | 19,66% | 24,51% | -24,32% | 27,84% | 26,41% | 0,61% |
| Europe | 14,24% | 16,58% | 12,41% | -23,60% | 12,75% | 17,63% | -4,87% |
| Commonwealth of Independent States | 27,61% | 26,10% | 34,58% | -35,28% | 28,83% | 32,69% | 2,89% |
| Asia | 16,27% | 15,23% | 16,87% | -18,60% | 31,42% | 20,09% | 3,31% |
| Others | 21,15% | 18,83% | 31,00% | -25,11% | 24,16% | 25,55% | 4,80% |
| European Union (27) | 14,07% | 16,35% | 11,88% | -23,62% | 12,50% | 17,24% | -5,23% |
| Intra-trade | 13,84% | 16,39% | 9,88% | -23,54% | 9,88% | 15,92% | -6,93% |
| Extra-trade | 14,54% | 16,29% | 15,83% | -23,76% | 17,45% | 19,55% | -2,34% |

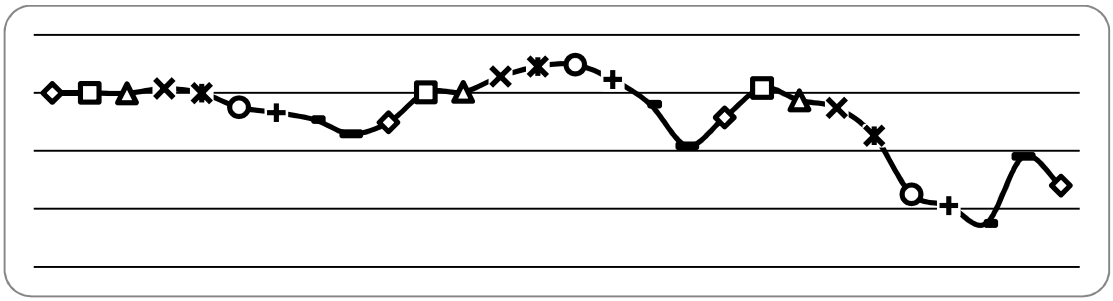
*Source: Eurostat, Comext Database; National statistics; Global Trade Atlas; IMF, International Financial Statistics. http://www.wto.org/english/res_e/statis_e/quarterly_world_exp_e.htm*

Regarding the regions, the exceptional decrease was noticed in the Commonwealth of Independent States (C.I.S) of 35.28% in 2009, while the region of Asia has the lowest slowdown in the volume of trade of 18,6% on annual basic. Still, the decline in the trade has high degree of synchronization across countries, as a result of the developed and closely connected financial market and transmission power of the informational technologies.

The downfall of the total trade of EU was 23,62% in 2009 compared with 2008. The declining foreign demand in the wake of the 2008/09 global economic downturn hit the EU' export sector particularly hard. This led to increasing concerns about the prospects for EU` exports and competitiveness, particularly at a time when exporters had already been struggling to adjust to the fiercer competition and other structural changes resulting from globalization. While partly reflecting the relatively high openness of the European economy, this has also prompted increasing concerns about the competitiveness of the Union.

Trends in exports and imports may serve to calculate the value of the current account of the European Union. Trade balance of Union in the reviewed period had a mainly negative value , i.e. value of imports is higher than the value of export and is worsening over the last decade. Since 2002 the trade deficit is widening, and it reached the highest negative value in 2008 (525,1 billion Euros). The recovery was in 2009, when the trade balance showed positive tendencies. According to the data from Euro stat only in the period 1993-1998, the EU exerted a positive trade balance (figure 1).

*Figure 1. Trade balance of EU (billions euros/ECU)*



*Source: Eurostat, (2011): External and intra-EU trade: A statistical yearbook, data 1958 – 2010, European Commission, Luxemburg, *the data cannot be consistent on the yearly intervals because of the lack of data*

So far, European policymakers seem to have watched the growing imbalances without much concern, in the hope that the EU will be largely unaffected (Ahearne, Jürgen, 2005). Additionally, the trade account balance, as well as the current account balance has never constituted a condition for acceptance of a single currency. Even in Maastricht criteria for entry in the Euro zone, there are no restrictions on trade or current account deficit. Under Article 143 of the Treaty on the Functioning of the European Union, only countries - countries that have not yet adopted the euro may receive financial assistance to deal with have problems in the balance of payments *(Treaty of the functioning of the European Union*).

The reason why the EU does not allow for funding the deficit in the trade account is because it is considered that no economy cannot be exposed to speculative attacks of the common currency. Therefore, deficits between countries that are already members of Euro

zone should be financed through short-term financial markets, without the need for intervention by the monetary authorities.

The problem is systematic. The trade deficit of the EU is a result from the countries that traditionally achieve trade surplus (Luxembourg, Finland, the Netherlands and Germany) and countries with traditionally high deficits (Greece, Portugal and Spain). However, the deficit in the trade account of Greece, Portugal and Spain was balanced until the mid- 1990s. Obviously, the process of convergence of these countries in the monetary union impacted negatively on the country, resulting in deepening deficit due process of adaptation to the EU. Just for example, the Spain balance of trade increased in 2006 approximately four times more compared in 1999 (Trading Economics database).

Interesting is that the crisis created cyclical movements in the trade balance of the EU countries. The countries that traditionally have trade surplus, experienced lowering of the trade balance, and vice versa for the countries with the trade deficit. By approaching price and cost competitiveness this research will try to give an answer to these problems.

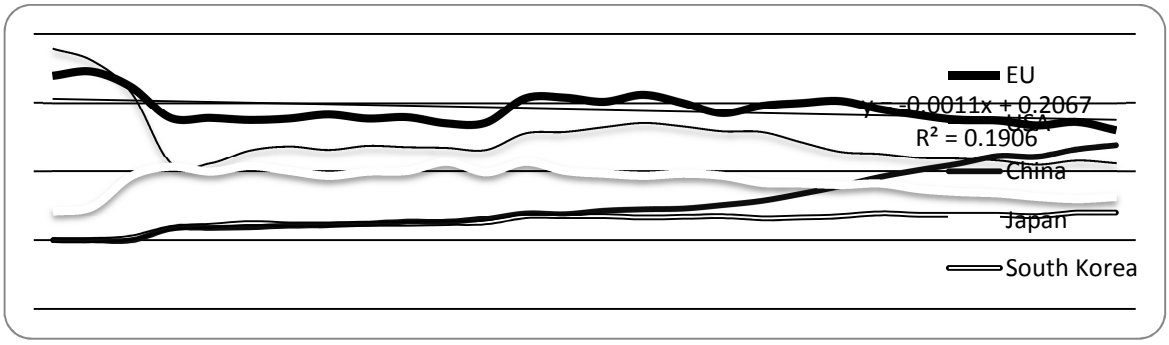
## Approaching price and cost competiveness of the EU

Competitiveness of the EU as a main global trade leader is achieved by the advantages of the existence of the common market. The EU is the world`s largest exporter with well positioning in the global value chain. Still, the common market of the EU is fragmented by the domestic producers that do not use the advantages of the economies of scale as a result of not synchronized policies. With the beginning of the economic crisis, many of the structural weaknesses of the Union were revealed. As the private demand remain resilient and the public expenditure increased the internal imbalance of the Union. Slugging international demand and poor economic outlook limited the potential for export.

The trends of the export of the EU is moving almost in the same direction as the total trade of the EU. Export growth reached its peak in 2007 with 17% annual growth, and experienced decline in 2009 of 23%, compared with 2008. After the short recovery the export showed 5% decrease in 2012 compared to the previous year.

According to the share of the export of the EU in the world export, the relative indicator is slowing down (figure 2). With the exception of the period 1958-1960, the Union had the highest share in the value of world exports in the whole observed period. In 1996, EU had a 20.8% market share of the world trade in goods (excluding intra-EU). This market share has been lowered by competitive pressures from emerging economies, falling to 16% in 2010. The second largest world exporter were USA, whose share has been declining gradually since 2000. The most remarkable development is that China as fastest growing economy from 2005 onwards become the third largest exporter in the world, followed by Japan as the fourth largest world exporter. Thus, if we make comparison, we can see that the rise in the export share of China for 10 p.p. from 1996 to 2010, has been fairly affected by the EU (fall of 4,8 p.p.), USA (4,6 p.p.) and Japan (3,7 p.p.) over the same period.

*Figure 2. Participation of the countries in the total world export of goods*



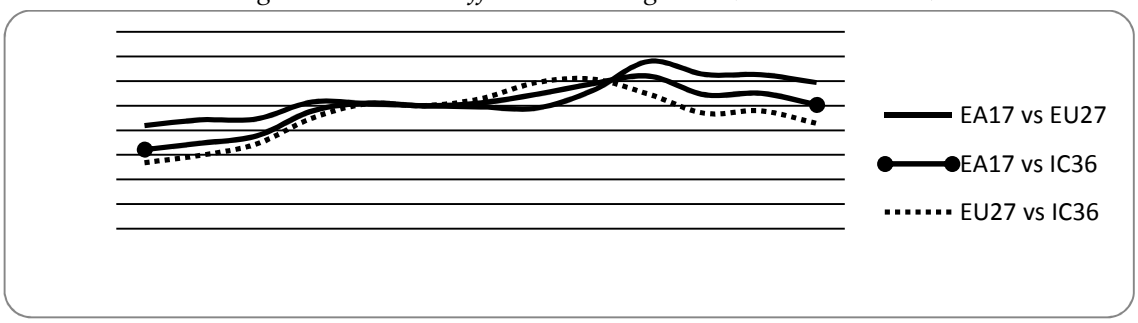

*Source: Eurostat, (2011): External and intra-EU trade: A statistical yearbook, data 1958 – 2010, European Commission, Luxemburg, *the data cannot be consistent on the yearly intervals because of the lack of data*

The EU's export performance varies significantly between markets. The EU shows a decrease in market shares on some of the most dynamic importing markets during the last decade. The largest gain is in the USA market, where the EU accounted for over one fifth of the import market in 2007. This performance coincided with shrinking shares of Japanese and to a lesser extent, of Canadian and ASEAN exports in the same market. Conversely, the EU loses market shares on the BRICs markets. The small market share loss of EU products on the rapidly expanding Chinese market could, however, have a large impact in the long run.

This appears to be mainly associated with the unfavorable trends in price competitiveness of the EU. Measured in terms of relative export prices, European Central Bank estimates that the euro area price competitiveness deteriorate by around 10% between 1999 and 2008 (ECB, 2010).

The decrease in the price competitiveness is confirmed by the movements of the nominal effective exchange rate, given in figure 3. An increase of this indicator suggest an appreciation, which indicated lowering of the price competitiveness. The appreciation of the exchange rate was from 2002 to 2009, after it experienced depreciation until 2012. The figure show that the Euro zone has lower price competitiveness compared with the EU as an economy of 27 member countries (not taking into consideration Croatia, because of the lack of data).

*Figure 3. Nominal effective exchange rate (index 2005=100)*

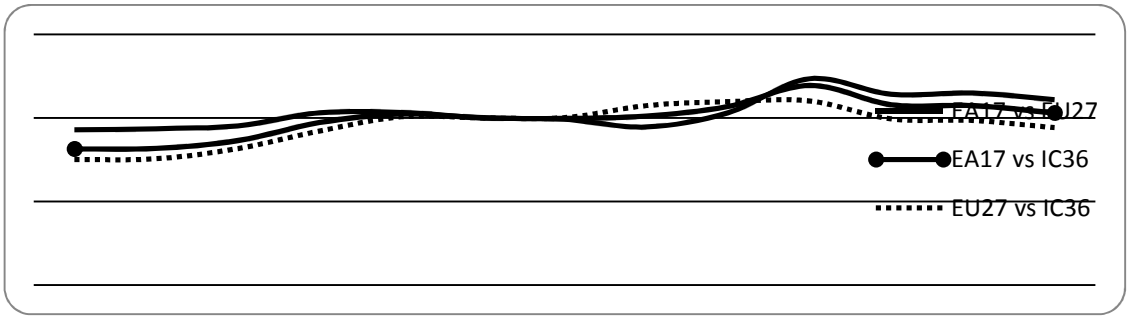



*Source: European Commission,*
*http://ec.europa.eu/economy_finance/db_indicators/competitiveness/data_section_en.htm*
** IC 36 = group of 36 industrial countries*

Still, the price competitiveness differs from country to country. High price competitiveness is achieved for Germany, France, Austria and Finland. Losses in price competitiveness is recorded in most of the countries - were at the same time experienced decline in the export - Estonia. Malta, Cyprus, Greece.

The losses in market shares have coincided with a degradation of cost competitiveness, measured by the Unit labor costs. The rise in the real effective exchange rate indicate lowering of the cost competitiveness. As a consequence of the strong growth of real wages since 2002 in most of the countries, ULC has increased both in the EU and euro area as a whole (figure 4).

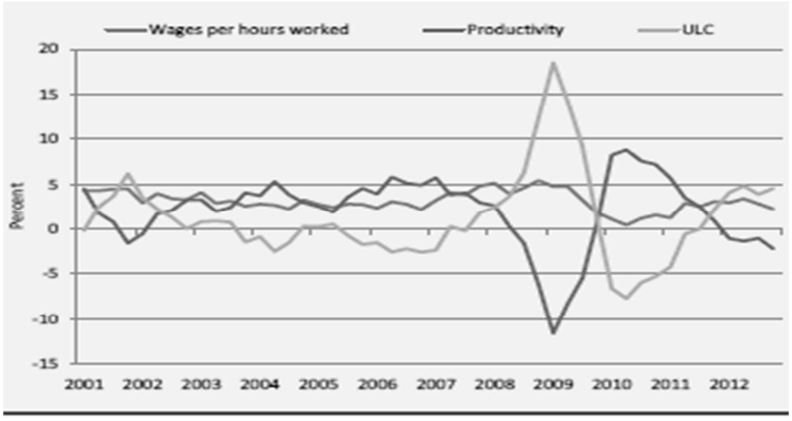
*Figure 4. Real effective exchange rate (ULC) (index 2005=100)*




*Source: European Commission, http://ec.europa.eu/economy_finance/db_indicators/competitiveness/data_section_en.htm*

Despite the intensive wage growth which is a long term trend, during the whole period from 2002-2011, the peripheral member states register high unemployment rate, which indicates low wage sensitivity to the unemployment movements (figure 5). Additionally the cyclical effect of the crisis caused losses in the labor productivity, meaning faster decline of output relative to employment during the slump. Between the first quarters of 2008 and 2009, production decreased by 19% while hours worked fell by 8%. (European Commission. 2013).

*Figure 5. Fluctuations in EU ULC are mainly caused by variations in labor productivity growth*




*Source: European Commission, (2013): European Competitiveness Report 2013:Toward knowledge driven reindustrialization, European Commission, Commission Staff Working Document SWD(2013)347 final, p.28*

Therefore, as a result of the insufficient labor productivity achievements, despite the introduction of new technologies and good business practices, the economic growth in the Union was slowing down. In other words EU is not an optimal currency area, except the lack of wage flexibility, the EU does not have convergence in the business cycles, has low mobility of labor force and capital. In this regard, it can be concluded that in the event of economic shock, when there is no flexible foreign exchange regime and autonomous monetary policy in the member states, the labor mobility or wage flexibility cannot recover the differences among the economies in the Monetary Union (Trpeski, Kondratenko, Jankoski, 2013).

Therefore there is limited potential growth of national spillovers. This argument is supported by the Regional Competitiveness Index (RCI) calculated by the European Commission, which measures the different dimensions of competitiveness at the regional level in EU countries. RCI reveals substantial differences in competitiveness within some countries. In France, Spain, the United Kingdom, the Slovak Republic, Romania, Sweden and Greece the level of variability across regions is particularly high. Thus, large gap in regional competitiveness is harmful for national competitiveness and consequently for the Union as a whole (The World Economic Forum, 2014).

## Non- price competitiveness

While for most EU countries price competitiveness has been a critical factor in shaping relative export performance with respect to major direct competitors – most notably developed economies – other non price-related factors play a part. Generally, non-price competitiveness comprises the structural and technological aspects of competitiveness. In this context, factors such as research and innovation, infrastructures, as well as the regulatory and tax framework of a country, are critical because they affect the prospects of achieving higher productivity growth and thus competitiveness in the medium and longer term (ECB, 2010).

The European Competitiveness Report (2013) shows that the EU has comparative advantages in most manufacturing sectors (15 out of 23) accounting for about three quarters of EU manufacturing output. They include vital high-tech and medium-high-tech sectors such as pharmaceuticals, chemicals, vehicles, machinery, and other transport equipment (which includes aerospace). In the high tech sectors, the EU has comparative advantage in pharmaceuticals but lags behind in the rest of this broad category (computers, electronics, and optical equipment). Even in the medium high-tech sectors, EU comparative advantage is lower than for the US and Japan. More importantly, China and the other emerging industrial economies are quickly gaining ground in the knowledge intensive sectors and rather than merely assembling high-technology products they are now producing them. Even though the data in table 2 confirm that the China is a leader in high tech industries, still this is not a reliable data. It is a result of the offshore activities of the USA and EU for a low cost production.

*Table 2. Comparative advantage by technology intensities in manufacturing, 2011*

| | High tech | Medium high tech | Medium low tech | Low tech |
|---|---|---|---|---|
| EU | 0,85 | 1,14 | 0,89 | 1,01 |
| Japan | 0,73 | 1,59 | 0,86 | 0,16 |
| USA | 0,88 | 1,22 | 0,96 | 0,68 |
| Brazil | 0,32 | 0,76 | 0,87 | 2,5 |
| China | 1,56 | 0,72 | 0,85 | 1,29 |
| India | 0,4 | 0,49 | 1,93 | 1,33 |
| Russia | 0,08 | 0,45 | 2,74 | 0,49 |

*Source: UN Comtrade*

The type of specialization of the countries can explain the cyclical movements in the trade balance. Since, there is a difference between elasticity of different categories of goods and services, trade in services, except for transport, declined with less dynamics than trade in goods. In the trade in goods investment good register the greatest reduction. Contrary to these trends, the trade of traditional "un cyclical" sectors, such as food, beverages and pharmaceutical products, was far more resilient.

Consequently, countries that entered the global economic crisis with large trade deficits had a significant improvement in the condition of the trade account during the 2008 - 2010. Countries that had substantial trade surpluses had note lowering of the positive balance in the trade. This suggests that the decline in trade surplus of the countries that traditionally generate a positive trade balance (Germany, France, Austria, Belgium and Netherland) is due to the elasticity of world demand for capital intensive products and investment goods, in which these countries are highly specialized. Conversely, countries with trade deficits (Greece, Spain, Cyprus, Slovenia and Finland) that have high specialization in consumer goods, had slightly reduced exports due to the global "un elasticity" demand (Mauro, Foster, Lima, 2010).

These developments are cyclical, i.e. they are occurring due to the impact of the economic cycle in which the world economy is. Thus, after the crisis, current trends in the trade balance will be present again. Consequently, the existence of different economic structures of the countries is a systemic problem for the Union . Although it can be equated with the imbalance globally, there is a significant difference. Globally, the adjustment are achieved through exchange rate movements, while within the monetary union (such as the EU) that must be achieved through fiscal adjustment and coordination of policies within the member countries (Mrak, 2010).

We believe that decreased labor productivity of the Union is important and influence negatively not only for price, but also for non-price competitiveness. Labor productivity, and especially multi-factor productivity, is often seen as indicator of technical progress. Increased labour productivity means more output is produced with less labor, which can be due to technological or organizational improvements and other non-observable factors.

## Reasons behind loss of the EU competitiveness

In order to explain why European growth came down from the extraordinary levels it reached during the Golden Age (1950-1973), and most importantly the technological lagging of EU behind USA we will compare the indicators of labor productivity and labor input between EU and USA.

*Table 3. Levels of EU-15 relative to the USA, in PPP, (USA=100)*

| | 1950 | 1973 | 1995 | 2004 |
|---|---|---|---|---|
| GDP per capita | 45,5 | 76,8 | 74,9 | 74,1 |
| GDP per working hour (labor productivity) | 39,5 | 75,4 | 98,3 | 90,3 |
| Working hours per head of population (labor input) | 115,2 | 101,9 | 76,2 | 82,1 |

*Source: Ark, van B., O'Mahony, M., Timmer, P. M., (2008) "The Productivity Gap between Europe and the United States: Trends and Causes", Journal of Economic Perspectives, Volume 22, Number 1, Pages 25–44*

According to the numbers in the table 3, the problem is ascribed entirely to a relative fall in labor input (from index of 115,2 in 1950 to 76,2 in 1995 and 82,2 in 2004 compared with the USA). The reason for this is:

a) the ratio of population of employed to the population of working age is higher in USA 74% (OECD database) compared with EU of 68% (Euro stat database) . The data shows that are that employment rate (age group 20-64) is still below the objectives set in "Europe 2020" of 75% of the population.

b) The structure of the working population has aged considerably in recent decades. Between the 1960 and 2000 the average dependency ratio (defined as number of persons aged 60 or more years per 100 persons aged 15-59 years) for the EU-15 rose from 26 to 35. At the same time, the dependency ratio for the United States remained almost constant at around 25. During the period 1995-2015, the population above the standard retirement age, 65 years, will increase by 17 million (30%). Within this group the very old, those over 80, will increase by 5.5 million or 39% (Blanchard, 2004).

**c)** fall of the utilization rate of labor in Europe compared with USA which is a result of the sustainable preference for leisure due to the higher social protection of the workers and also by the labor rigidness of the European market.

Taking into consideration that the average hours worked are much shorter in EU and the employment rate is much lower compared with the USA, we can get artificially boosted indicator of the productivity. As the data show the productivity in EU did not decrease, just opposite the index GDP per working hour increase from 75,4 in 1975 to 98,3 in 1995. Then decreased to 90,3 in 2004, but still remain below USA (index=100) (table 2). This indicator should be revised in order to compare the real productivity gap between EU and USA. According to Cette (2004), the European productivity level should be revised downwards, which suggest that the productivity gap between EU and USA remain substantial.

The main turning point for widening the productivity gap is considered to be since 1995. Taking into account indicators of annual productivity growth, in the USA, average annual labor productivity growth accelerated from 1.2 percent during the period 1973–95 to 2.3

percent during 1995–2006. Comparing the same two time periods, annual labor productivity growth in the European Union declined from 2.4 to 1.5 percent (Ark, O'Mahony, Timmer, 2008). In the mid-1990s, there was a burst of higher productivity in industries producing information and communications technology equipment (ICT), and a capital-deepening effect from investing in information and communications technology assets across the economy. In turn, these changes were driven by the rapid pace of innovation in information and communications technologies, fuelled by the precipitous and continuing fall in semiconductor prices. Europe has been lagging behind the USA not only in ICT investment but also in total productivity growth in ICT producing as well as ICT - using industries.

Practically, the period of the two oil shocks 1973-'74 and 1978-'79 marked the end of the fast growing industries like chemical and automotive industry, production of plastics and artificial fibers, which have been the main driving force of economic growth in the postwar period. For thirty years, between 1950 and 1973 Europe enjoyed a "Golden age" of growth, stability and social cohesion.

All industries were replaced by new industrial sectors with high added value, such as electronics, chemicals and pharmaceuticals, computer technology and telecommunications. Although newly industrialized economies-Japan and "economies - tigers" of Southeast Asia, at that time were trying to increase the competitiveness of these industries, especially electronic, still in the information technology products and bio pharmaceutical products USA, had a big competitive advantage (Dyker, 1999).

Also, EU is lagging in the investment in research and development (R&D). According to the objectives set out by the European Commission (2010a), "Europe 2020", each EU should consider costs for R&D to be amounted 3 % of its national GDP (same as in the Lisbon strategy). In the period 1995 - 2010, the cost of R&D calculated as a percentage of GDP in the EU and the euro area are relatively fixed, and moving with an average value of 1.8 % of GDP, which is below the set limit.

EU and the euro area have only a higher spending rate on R&D than China. Within the EU, only Sweden and Finland with 3.7 % exceeding the target. Other countries that have a higher than average rate of union are: Germany (2.69 %) and Denmark (2.85 %). In 2008, Japan had the highest percentage of allocation of 3.45 %, followed by South Korea with 3.36 % and 2.76 % in the USA. South Korea has significant rise in the cost during the reporting period.

It seems that the Lisbon strategy for making the EU the world's most competitive economy is a failure. Still, an extension of the failed approach is in the works. After Lisbon strategy, The Europe 2020 strategy has emerged with some principle tasks, but central ideas of the Lisbon Strategy have been kept. The Lisbon answer has been the "open method of coordination. It was to aim at the middle ground, where key policy domains remain a national competence but are recognized as being of common interest. EU continue with the Lisbon-type reforms and developed new instruments of economic governance, especially with the beginning of the economic crisis.

Some authors (Wyplosz, 2010) state that Lisbon strategy should die a peaceful death and that a brand new model is needed. We believe that the model is adequate, even though there is no explicit productivity growth target formulated in the Europe 2020 strategy, but trends in labor productivity are monitored as one of its main indicators. The countries from EU

need to find their own ways of adjusting to the opportunities and dislocations of the new information and communications technologies. We believe that large extent of the reforms should remain under the member states` authority, which can bring higher incentive for its implementation, thus contributing to accomplish common interest. When one country becomes more productive, it benefits (through demand) the whole EU and raise the productivity of the rest of the countries. There also, need to be ensure greater labor mobility and flexibility of the common market, that can help the Union to improve the competitiveness and also to be able to face adverse shocks in the future much easier.

## Conclusion

Data for foreign trade of the EU show that the integration process and the introduction of the euro had contributed for the Union to become the biggest "trade player " in the world. However, there has been a gradual of trading positions of the EU. That is not only a result of the economic crisis, but due to the major structural weaknesses (shortcomings) of the EU.

In other words, the situation in the foreign account is created due to the gap in productivity, which led to a real depreciation of the exchange rate in favor of countries that have traditionally been exercising surplus. At the same time, most of the other Member States of the EU realized permanent foreign trade deficit that, among other things, was a result of the large discrepancy between labor productivity and wages, whose ultimate effect was perceived in shrinking or stagnant rates of economic growth of these countries.

It turned out that the economy of EU has a series of structural inconsistencies and numerous drawbacks in its economic system. The lack of compliance of the internal policies, was one of the most important reasons for the occurrence of asymmetric shocks in the Union, reducing the competitiveness of the economy EU and strengthening the negative effects from the existing economic crisis.

Among the Member States of the EU was created gap in prices for homogenous products. Even thought, the purpose of the single market was to allow free movement of goods, service, capital and labor, the goal was not met due to different price levels. The difference in prices and production costs have caused a negative impact on trade flows in the Union. EU shows a decrease in market shares on some of the most dynamic importing markets during the last decade, especially ASEAN market. The orientation of the trade towards the emerging countries can be suggestion for the rest of the member states for faster out of the crisis and balanced trade account in the future.

But on the other hand it is needed to boost the trade relations between EU countries in order to gain and improve the trade conditions in the Common Market. Long-term expectations and needs for the Common Market is to make a comprehensive structural changes in order to overcome structural differences between individual Member States to increase the overall competitiveness and individual, to remove trade barriers between individual Member States and to achieve higher individual and aggregate rates of economic growth. It is clear that the effects of deep integration of the EU has not yet been achieved, and expected benefits may not be realized, if the internal and external balance of the Union is not achieved.

According to our opinion, the EU needs changes in the long term strategy which should be oriented towards targeting specific systematic problems of individual member states of EU. The reforms need to be make in order to enhance competitiveness, seen as a priority. When one country becomes more productive, it benefits (through demand) the whole EU and raise the productivity of the rest of the countries. Even thought the relationship between labor productivity and market share gain is not straightforward, we tried to point out that decreased labor productivity growth in the case of EU influence on the declining share of the world market. Firms and industries from EU are facing tough competition from low-cost producers (especially from the Asian countries) and therefore they are forced to rationalized their production in order to survive. In that direction, the measures need to be oriented towards decrease in the employees` protection and higher initiative for regional and mobility of the labor force.

Additionally, if the competitiveness of the Union is not improved, the balance in the trade account will be provided by increased unemployment, particularly in certain sectors which are uncompetitive. That would mean risk of structural unemployment, i.e. more emphatic social crisis that could turn into a political crisis.

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# Konkurentnost Evropske unije: Trendovi pre krize i uticaj finansijske krize

***REZIME** – Cilj rada je da se ukaže na rizike od smanjenja konkurentnosti EU analizirajući pokazatelje cene koštanja i konkurentnosti, kao i strukturne i tehnološke aspekte konkurentnosti. Uticaj svetske krize na konkurentnost i izvozne performanse EU je sve više u fokusu kako bi se ukazalo na to koliko globalna kriza može da otežа već postojeće potrebe za sanacijom funkcionisanja Unije. Ne samo da je kriza pokazala da problemi u Uniji nisu nedavno nastali, već je nametnula hitne potrebe za poboljšanje nove politike kako bi povratila snagu konkurentnosti i performansi.*

*Preformulisana strategija treba da se zasniva na otvorenosti i inovacijama, uz ulaganja u istraživanje i razvoj. Dugoročny očekivanja treba da budu sveobuhvatne strukturne promene u cilju prevazilaženja strukturnih razlika između pojedinih država članica i povećanje ukupne konkurentnosti. Pored toga, neophodno je i da se uklone trgovinske barijere pojedinih država članica kao i da se postignu više pojedinačne i ukupne stope privrednog rasta. Jasno je da još uvek nisu postignuti efekti duboke integracije u EU, a očekivane koristi ne mogu se realizovati ukoliko se interni i eksterni bilans Unije ne održava.*

***KLJUČNE REČI***: *globalizacija, internacionalizacija, biznis, globalna tržišta, ekonomska integracija*

*Article history:* Received: 8 September 2014
Accepted: 23 November 2014