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Why Draghi's Plan For Europe Will Likely Fail



Most financial media have received Mario Draghi's **document** on the future of Europe's competitiveness with enthusiasm this week. However, it is the recipe for secular stagnation.

After the unmitigated failure of the Growth and Employment Plan of 2009, the Juncker Plan, and the Next Generation EU Plan, he recommends doing the same, but on a grand scale.

The Draghi report looks at the United States and China and assumes that what gives them leadership is enormous spending and a significant deal of public intervention, which is what holds back their potential.

The United States and China are not leaders because of their central planning or because they spend a lot, but because they reward success and allow creative destruction and entrepreneurship to create wealth.

The document provides an impeccable diagnosis. The European Union is suffocated by excessive regulation, high taxes, a lack of coordination, and disincentives to investment.

Is there a solution to the interventionism and bureaucratization of the European Union? Draghi proposes more central planning and spending.

Giants with privileged access to capital markets

It is wrong to believe that greater centralization and a massive, urgent increase in public and private capital focused on large companies will lead to better investment.

Could you envision a centralized European investment policy in technology and energy in 2012? Today the European Union would not be in stagnation, it would be in depression.

The European companies that Draghi places at the forefront of the bet on innovation and technology were giants with privileged access

to capital markets three decades ago, but none invested, not even through acquisitions, in what are now American tech giants.

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Many of these European companies, attempting to maintain their status as national champions, have fallen behind in the technology race, dedicating hundreds of billions of euros to value-destructive acquisitions driven by megalomaniacal supranational aspirations suggested by political power.

To assume that those companies will compete with the U.S. by uniting politicians and crony sectors is simply delusional.

Defense and energy

The report makes a mistaken analysis of defense investment and technology.

Europe is not lagging in technological leadership because it spends little on defense, but rather because a political system prevents the emergence of incentives and systems of reward and punishment.

Spending more on tanks is probably necessary, but you'll never have a Tesla, a Netflix, or an Amazon if a group of political and economic elites is in charge.

Netflix would never have gone beyond being a DVD rental service by mail, nor would Amazon have evolved from a book-selling service if the European political and economic power system were in charge.

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Spending more on defense is a necessary condition due to security factors, but it is not sufficient to lead in technology. Israel understands it perfectly. Once there is a patent or an innovative idea, they privatize it and take the project to public markets. That would never happen in Europe.

In energy, it's the same. The European system penalizes success through taxation and blocks the necessary creative destruction, generating zombie dinosaurs. Large capital sums financed with debt and money printing will not solve this problem.

The state does not innovate

Draghi seems to want to buy into Mazzucato's fallacy of the entrepreneurial state. However, this misguided perspective conflates the state as a co-financier with the state machinery, which includes regulated companies, as creators and innovators.

The state does not innovate, it absorbs wealth. I recommend "The Myth of the Entrepreneurial State" by McCluskey and Mingardi.

Draghi neglects to mention in the report that one of Europe's major problems, when compared to the United States, stems precisely from the public-private identity and the closeness of certain companies, now dinosaurs, to governments.

The European Union has been a chain of multi-trillion stimulus plans

The report aligns with the common errors made by investment bankers: Assuming that the problem is the amount spent. Is Europe

not progressing because it doesn't spend enough and lacks sufficient central planning? Not at all.

The European Union has been a chain of multi-trillion stimulus plans. Draghi only attributes the failure to a supposed dispersion among member states, as if concentrating them in a central planning group would have made it better. The exact opposite.

The museum of zombie businesses

In **monetary policy**, the ECB's balance sheet is almost double in relation to GDP compared to that of the Federal Reserve. The ECB's balance sheet reached a peak of 68% of GDP and it is at 44%, while the Fed's went up to 37% and is at 25% today.

The ECB implemented negative nominal rates and significantly increased debt monetization, leading to the ongoing decline of the eurozone.



The EU leaders will implement Draghi's plan, and in ten years, we will ask ourselves why the EU is the world's museum and a wasteland of zombie businesses - Daniel Lacalle

After accurately diagnosing the excess of normativism, regulation, and taxes, Draghi recommends increased spending and the issuance of mutualized debt, thereby exacerbating fiscal irresponsibility.

Another element ignored by the Draghi report is that China's excess capacity problem stems

precisely from central planning, whereas its technological leadership began with "loans" of American intellectual property (over \$225 billion annually, according to the U.S. Congress).

It is also worth noting that China's remarkable growth has come from openness, private ownership, and free enterprise, which rewards the creation of wealth.

The problem in Europe is not a lack of public spending or monetary stimulus. The problem is a bureaucratic system that fiscally penalizes success and subsidizes failure to perpetuate a crony business system that is dependent on the government.

The EU leaders will agree and implement Draghi's plan, and in ten years, we will ask ourselves why the European Union is the world's museum and a wasteland of zombie businesses. Furthermore, it's highly likely that someone will suggest further interventionism as a solution.