EUROPANOVA

HOW EUROPE CAN RECLAIM THE TECH REVOLUTION

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As the founder and CEO of a tech startup based in Paris, I pitched our innovative solution to a major European bank. Their primary question was: “Has it already been proven in the US?” A few months later, I presented the same solution to a leading American bank. Their key question: “Will $1 million be enough for a pilot?”

Why do we encounter such contrasting reactions from similar customers on opposite sides of the Atlantic? Is it due to a lack of money in Europe? No, both banks are highly profitable. Is it because of the fragmentation of the European market? No, both banks are of comparable size and operate across multiple countries. Is it a lack of public funding? No, that's irrelevant in this sector. Could it be a weak risk culture in Europe? Perhaps, but why? After all, Europe led the world in risk-taking and technological innovation from 1450 to 1940. So, what has changed?

I’ve founded three startups in Paris, developed cutting-edge tech solutions, and attempted to gain traction with European customers. Instead, we received unsolicited calls from U.S. giants like Microsoft, Dish, and IBM, who quickly adopted our solutions. Before long, over 95% of our revenue came from U.S. clients. Why is that? I spent the past two years trying to answer this question by examining Europe’s position in tech, and I was stunned by what I discovered—again and again.

In Information and Communication Technologies (“tech”), European companies invest €50 billion annually in Research and Development (R&D)—six times less than their American counterparts, who invest €300 billion. With such a significant gap, Europe is unlikely to create the next Apple, Google, or OpenAI. Interestingly, European companies outspend their U.S. competitors in R&D in non-tech sectors like automotive, aeronautics, chemicals, and energy. Furthermore, public R&D funding and government support are roughly equal between the U.S. and Europe, suggesting that Europe’s lag in tech isn’t due to weaker public backing. Nobel laureate Jean Tirole reached a similar conclusion: public innovation spending is comparable on both sides of the Atlantic, while governance and strategic focus need improvement in Europe.

What makes tech so fundamentally different from other industries? Philippe Camus, former CEO of Airbus and later Chairman of Alcatel-Lucent once shared his surprise at discovering the short life cycles of telecom products compared to the long cycles of Airbus aircraft. Tech is inherently volatile: we’ve seen booming activities collapse by 99% within a single quarter. It’s also unpredictable: even within giants like Amazon,

Google, Meta, or Microsoft, only 1 in 5 projects succeeds, with the rest being scrapped after months or years of intense effort.

Volatility and unpredictability are hallmarks of any industrial revolution. In 1900, France and Germany saw hundreds of startups developing automobiles, driving the second industrial revolution. After 30 years of volatility and uncertainty, the European industry consolidated into six major manufacturers that dominated for nearly a century. Today, the same buzzing creativity is unfolding in the tech sector, with startups becoming global champions in less than two decades—like Uber, Facebook, or Alibaba. Yet, this tech revolution is happening in the U.S. and China, not in Europe. Why?

In the 1970s, Europe introduced Employment Protection Laws to shield blue-collar workers from the mass layoffs triggered by the first oil shock. For over 50 years, these laws have also applied to well-paid engineers and highly skilled sales professionals. When faced with failures or downturns, large companies in Europe endure substantial restructuring costs due to long delays and high severance packages. In countries like Germany, France, Italy, and the UK, the 'cost of failure' can equal years of compensation, whereas in the U.S., China, India, Denmark, and Switzerland, it amounts to just months. Our analysis shows that these high costs stifle profitability on risky investments for large corporations, which is why Europe remains specialized in industries from the second industrial revolution, while the U.S. and China have surged ahead in tech.

Our analysis also reveals that these costs of failure contribute to the lower profitability of European venture capital funds compared to their U.S. counterparts. This profitability gap directly impacts the availability of funding for scaling up European startups, which receive three times less capital than American startups.

Europe's weak performance in tech has significant consequences for the continent. According to the European Central Bank, it has led to a 20% decline in relative competitiveness compared to the U.S. over the past 25 years. Mario Draghi has warned that Europe is facing a “slow agony” unless it changes course. Even more alarming, Europe's security and defense capabilities are at risk without advancing in tech—it’s akin to preparing for World War II without internal combustion engines.

Political and industry leaders are hesitant to address Employment Protection Laws, fully aware of their political sensitivity. In most European countries, proposing an “American” social model is political suicide. Fortunately, Europe doesn’t need to adopt the U.S. approach to foster innovation. Viable solutions already exist within the European social model, as seen in Denmark and Switzerland. Moreover, there’s no need to challenge the

protections of 90% of employees—tech industries primarily employ highly skilled and well-compensated experts who are not at risk of mass unemployment.

We propose applying the Danish or Swiss flexicurity model to employees earning over €50,000 annually. Combining social justice with economic efficiency, such a reform would restore profitability for tech investments and could attract hundreds of billions of euros in R&D investment to Europe each year—all without further increasing government debt.

Mario Draghi highlighted the issue in his September report: “EU companies face higher restructuring costs compared to their US peers, which places them in a position of huge disadvantage in highly innovative sectors”. However, his proposal to invest $800 billion of public funds annually is neither realistic nor effective. It’s unrealistic because European governments lack the fiscal capacity. And it’s inefficient, given the low leverage effect of public money on private investment—1:1 in Europe compared to 10:1 in the U.S. The real priority is to restore the profitability of high-risk investments in Europe.

It's possible. Tackling the costs of failure for companies investing at risk could reinsert Europe into the current industrial revolution, raise our standards of living by 10 to 20%, generate hundreds of billions in additional tax revenue, and rebuild our security and defense capabilities. China transformed from an agrarian society into a tech powerhouse in just 40 years. The hill Europe has to climb is much smaller. It’s time for Europe to roar again.

For more on this, see:

- **Cost of Failure and Competitiveness in Disruptive Innovation**, Oliver Coste and Yann Coatanlem, Bocconi, September 2024
- **Europe, Tech and War**, Oliver Coste, Amazon, 2024
- **Why Europe is a Laggard in Tech**, Yann Coatanlem, Financial Times, February 2024
- **Tech: quand l’Europe s’éveillera,** Yann Coatanlem and Olivier Coste**,** Commentaire, December 2023