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Book Review

Book Review: Welfare and Employment in a United Europe

Aussenwirtschaft

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Suggested Citation: Feld, Lars P. (2002) : Book Review: Welfare and Employment in a United Europe, Aussenwirtschaft, ISSN 0004-8216, Universität St.Gallen, Schweizerisches Institut für Aussenwirtschaft und Angewandte Wirtschaftsforschung (SIAW-HSG), St.Gallen, Vol. 57, Iss. 1, pp. 105-108

This Version is available at:

<https://hdl.handle.net/10419/230997>

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Giuseppe, Bertola, Tito Boeri and Giuseppe Nicoletti (eds.)
Welfare and Employment in a United Europe
MIT Press, London 2001, 291 pages, 22.50 £.

The discussion about welfare and employment policies in the EU appears to have calmed down after the creation of EMU and the accompanying stability and growth pact. Remember that, in particular due to the efforts of the French delegation, a 'growth component' had to be included in the original pact that, at the start, only referred to stability (stability pact). Aimed at a relaxation of the provisions for sound public finances of the stability pact in the first place, the growth component demands member states of EMU to undertake common efforts to fight unemployment in Europe. But indeed little has been done to coordinate the actions of single member states in the employment and social policy field. Neither the stability and growth pact nor the social chapter of the Maastricht Treaty constitute a well-designed basis or even provide clear impulses for such a coordination of social and employment policies.

But this surface of calm only hides the political conflicts that still exist. Proponents of coordination or harmonization of social policies bemoan this current state of affairs in the EU. They argue that European monetary integration enforces locational competition between member states because product and factor prices, effective tax burdens and social benefits, hence all kinds of location advantages and disadvantages become comparable and transparent. Some of them fear such a locational competition because it is supposed to lead to a breakdown of the welfare state. Mobile production factors move to places where they pay – *ceteris paribus* – lower taxes while the poor either have to pay for the public sector or, if they are mobile too, they move to places where they obtain – *ceteris paribus* – higher transfer payments. Similar arguments can be made with respect to any form of government regulation.

Other authors believe that European product and factor markets are too rigid. The rigidity of product and factor prices is supposed to have led to low GDP growth, high unemployment and the postponing of necessary structural adjustments, all of it subsumed under the heading of 'Eurosclerosis'. While the first group of proponents of social policy coordination in the EU hopes for a preservation of the welfare state by harmonization, the second group believes that pressure from the EU in its coordination efforts leads to social policy reforms in member countries that are a precondition for a more favorable economic development in the future. And indeed the deregulation of product markets that has actually happened since the mid-eighties is at least partly a result of coordination activities of the EU in its goal to complete the four freedoms of the Common Market.

Opponents of harmonization in the social policy area are rather sceptical about the possibilities of obtaining major reform impulses from the EU. Instead, they fear that a collusion of member state governments at the EU level aims at a reduction of competitive pressure from abroad. This policy of 'raising rivals' costs' is designed to prevent structural adjustments from taking place. Labor market reforms are postponed for ever. According to these people, the only hope is a fierce competition between different countries to attract mobile capital. The competitive pressure supposedly forces national governments to reduce their public sectors to efficient sizes providing public services only at levels people and firms are willing to pay for. This locational competition urges countries to abolish inefficient and obsolete product and labor market regulations, reduces

market power of firms and interest groups that are powerful at the national levels only, and reduces the redistribution efforts of governments to the essentials.

While this description summarizes some of the discussion in the tax competition literature quite well, the broader perspective to social and regulatory policies in general is still in its infancy. The volume edited by BERTOLA, BOERI and NICOLETTI impressively fills this gap. The authors first nicely survey the theoretical discussion outlined above and apply it to social policies and regulation. Second, they present abundant evidence on the development of social and regulatory policies in EU countries. Third, they have a look at the impact of product and labor market regulation on labor market performance and employment composition in an econometric study. Finally, they empirically assess the implication of EMU for European product and labor markets. This volume is therefore a highly welcome and rich contribution to the debate about welfare and employment policies in Europe.

Unlike usual edited volumes, this is done in two larger chapters that are supplemented by comments, an introduction and an appendix. Thus, only two broader perspectives are opened on this debate leading to a stronger coherence of the book than it is usually achieved by conference volumes. TITO BOERI nicely introduces the reader to the discussion along similar lines as above. He also provides an empirical survey of the development of key social policy areas from the middle of the eighties to the end of the nineties which is wonderfully supplemented by the extensive appendix on social policy reforms in the end of the volume. Figures are provided on social security contributions, unemployment benefits, social assistance programs, employment protection legislation, and the relationship between GDP growth and major reforms in these fields since the eighties. His assessment of this descriptive exercise is intriguing: The development and reforms of social and regulatory policies do neither look to appear in a very rational way nor do they appear to have clear beneficial or deteriorating impacts on economic welfare. The introduction concludes with a call for studies that help to understand the complexity of the issue, provided, e.g., by the following chapters of the book.

After a more detailed assessment of the state of income inequality, poverty and social policies in EU member countries in the nineties, the first core chapter of the volume by BERTOLA, JIMENO, MARIMON and PISSARIDES contains a discussion as to whether European integration has already had a negative impact on European social welfare states. This part of the chapter underlines the variety and diversity of social policy programs across European countries. In order to reduce this complexity somewhat, the authors follow ESPING-ANDERSEN by distinguishing the four groups of Nordic, Continental, Anglo-Saxon and Southern European countries according to historical decisions for certain types of welfare states in Europe. This distinction appears to be useful because a clustering of member countries in those groups is possible with respect to their social policies during the nineties. While the authors clearly indicate, that the evidence for the breakdown of welfare states due to European integration is rather weak, they nevertheless take the threat that increased mobility of labor and capital poses to the welfare state seriously. Based on an insightful survey of the theoretical arguments in the field of systems competition, they therefore proceed by discussing the necessity of harmonization and coordination with respect to specific social policy programs. They underline the need for coordination starting from the fact that national lobbies will successfully oppose further integration steps when clear negative distributive consequences result from systems competition. European integration could thus be endangered by its very success.

Think of globalization opponents and the Genua street-fighting for examples corroborating this view. The authors suggest to impose minimum welfare standards across the EU for transfers and services guaranteeing a minimum welfare level to citizens, whereby benefits should be adjusted to reflect local price levels; to coordinate policies for contingent insurance provision at the EU level without allowing it to interfere centrally in their details or financing; and to allow for full competition in services (health care, day care and so on) as well as labor market institutions.

The main point emphasized by ESPING-ANDERSEN in his comments is that BERTOLA et al. suppress the role of the family as a social safety net. It is not simply the interaction of welfare, of social insurance systems for the old, the unemployed and the sick people and of services like day care that has to be considered. If the family is playing a more important role in one society than in another, harmonization efforts, be it only minimum standards, have to be seen in a different light. Too generous state transfer systems might erode a well functioning family based society. Also mobility has to be seen from a different perspective. A very incisive statement is: "Realistically speaking, do we know anything at all about the marginal utility of a 30 percent income gain against the loss of friends, family, language, and culture?" (p. 135). Consequently, many of BERTOLA et al.'s suggestion are too far-reaching for ESPING-ANDERSEN. He suggests to redirect resources to correct family failures like single parent families, separations and divorces. The much shorter discussion by ESPING-ANDERSEN finally appears to be slightly more sensitive to the pressing social problems in the different European countries than BERTOLA et al.

The second core chapter by NICOLETTI, HAFFNER, NICKELL, SCARPETTA and ZOEGA starts from a totally different perspective. It is aimed at providing insights as to whether European integration actually has had an impact on labor and product market regulation in Europe. First, the authors provide evidence for 19 OECD countries that stricter product and labor market regulation induced higher wage premia and lower employment, while labor market regulation also led to higher self-employment rates in the service sector. With a set of empirical findings the authors also support the hypothesis that European integration, in particular monetary coordination already during the EMS, was accompanied by deregulation and a higher flexibility in the adjustment to adverse economic shocks. NICOLETTI et al. underline the caveat that this is rather preliminary evidence given the fact that EMU is just three years old (and could simply not be evaluated at the time the paper was written). Nevertheless, the results are interesting and certainly stimulate future research along these lines. Particularly, it has to be noted that this is the first paper to my knowledge that really uses time variant indicators of labor market regulation to conduct an econometric panel data analysis although it is still only for the nineties decade. In his comment, BLANCHARD correctly emphasizes the high quality of the research presented in this paper, but also in the whole book. He clearly states that improvements in unemployment could be expected to a much larger extent from reducing unemployment benefits or labor market regulations than from product market deregulation.

In general, this book has to be strongly recommended to anyone who is interested in economic policy in the EU area. The book contains everything such a study needs. It copes with an interesting topic that was, is and will be highly debated by policy-makers. It is easily accessible to readers that do not have an economics major. The theoretical background is mostly provided in survey style without using much math and without incurring much higher costs in terms of losses of analytical rigor. Finally, the data present-

ted here are not unique, but the collection and way of provision certainly is. The book actually provides the interested reader with abundant empirical facts and figures. In addition, to my knowledge, it is the first empirical study linking the whole set of social and regulatory policies to European integration. It therefore fills an important gap in economic research. Since European integration has a long way to go, the volume could only provide the starting point for such an analysis. Some starting points are so fundamental that they become the basis for a whole line of research. This study has the potential for it.

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