

Divisive integration

The triumph of failed ideas in Europe — revisited

Edited by
Steffen Lehndorff

etui.

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Europe's divisive integration – an overview

Steffen Lehndorff

‘The worst of the crisis may be behind us, but this is not an invitation to be complacent. To make the recovery stronger and create more jobs, we need to stay on the course of economic reform.’

Olli Rehn, 25 February 2014 ¹

1. Introduction

When, after the immediate effects of the worldwide financial and economic crisis had been surmounted, a course was set for ‘austerity measures’ and ‘structural reform’ Nobel prize-winning US economist Paul Krugman (2010) characterised it as a ‘strange triumph of failed ideas’: ‘Free-market fundamentalists have been wrong about everything — yet they now dominate the political scene more thoroughly than ever.’ We found this formulation so apposite that we used it as the title of our first joint volume on the European crisis published by the ETUI.² But the story has continued. Many changes that were merely on the horizon in 2012 have, in the meantime, come to pass and in a series of countries the full extent of the upheavals is discernible only today. On one hand, economic developments in a few countries may promise some light at the end of the tunnel. At the same time, however, the centrifugal forces have grown stronger, especially within the Monetary Union, both economically and politically. The economic and social contours of our continent in the further course of this decade are now clearer. In response to this we present here a continuation of our 2012 volume: largely new country analyses, supplemented by analyses of the policies of the European Union (EU) and the challenges facing trade union strategy. The focus of the present

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1. Former vice president of the European Commission during the presentation of the economic forecast for 2014. Available at: http://europa.eu/rapid/press-release_SPEECH-14-159_en.htm
 2. See Lehndorff (2012). ‘We’ being a grouping of labour market researchers from 10 European countries who have cooperated in various research projects – recently in an EU project on the ‘Dynamics of national employment models’ – over the past 20 to 30 years (see, among others, Bosch, Lehndorff and Rubery 2009).

volume is the weight attributed to the different economic and social development paths in individual countries, and their interaction with the austerity regime established at EU level, which in fact is deepening the crisis rather than paving ways out of it. The most dangerous implication of this policy approach highlighted in the following chapters is that it is driving European countries apart—misleadingly in the name of ‘Europe’. This is what we call ‘divisive integration’.

Many critical analyses of the European crisis concern themselves with wrong turns taken at the EU level and with economic imbalances within the EU and the euro zone. The fear has become widespread that the Monetary Union will ultimately founder on these problems. However, in these discussions for the most part too little attention is paid to the role that economics and politics should play at the national level in the course of reorientation. The national level is decisive, however, because any impetus for change in the EU and in the euro zone will proceed from individual countries (or groups of countries). At the same time, attempts at change at the European level can be blocked or discredited by individual countries, causing them to run aground. It makes sense, if we are to understand the extent of the challenge better, to take a closer look at the economic and social problems of individual countries.

This is the message of the present volume: a gradual recovery from the chronic crisis in the EU is possible only if there is a change of course in individual countries that then triggers reactions in the policies of other countries and perturbations at the EU level. However, it is also clear that a change of course in individual countries in most cases is no longer feasible without a green light or at least toleration from the level of the European institutions. In the various chapters of this book this interlinking is examined from either the national or the EU level. In the rest of this introduction I shall try to outline the connections between the two sides, starting with the policies being pursued, with EU support, to overcome the current crisis.

2. The competition Union

The severe economic downturn of 2008/2009 seemed to have been surmounted successfully and a recovery had got under way in the second half of 2009, thanks primarily to the massive deployment of economic

stimulus packages that, not long beforehand, had been vilified as ‘watering-can policies’. It was at this point, however, that the crisis of the euro zone commenced. The straw that broke the camel’s back was the revised budget presented by the newly installed Greek government. It came out that the public debt and the budget deficit were much higher than had been publicly professed. When one considers that Greece’s share in the EU’s economic output was at that time 1.8 per cent – it is now even smaller – it beggars belief that the announcement set off an avalanche that brought the European Monetary Union to the brink of collapse. What, then, is the problem?

The accepted wisdom is that the fortunes of each member country of the European Monetary Union are in their own hands. Mutual assistance was originally expressly ruled out (which officially is still the case, under the vigilant gaze of the Bundesbank and the German Constitutional Court). If ‘the markets’ purchase government bonds of particular countries only if, due to ‘lack of confidence’ in their economies, they receive high interest rates in return, other countries were not allowed to help out the relevant ‘debt sinner’ to ameliorate their acute financing problems. The economic journalist Thomas Fricke (2013: 63) has called this logic, which underlies the euro, the ‘Swabian housewife theorem’ (SHT): ‘Falling ratings and high interest rates on government bonds [were] the just punishment meted out by the financial markets to SHT sinners’. The governments affected must therefore make efforts to put their budgets in order in order to ‘restore the confidence of the markets’. Obviously, if that does not succeed straightaway and if in fact the economically stronger member states do not jump in to help immediately ‘the markets’ become distrustful and even more borderline cases emerge within the Monetary Union. Once ‘confidence’ has been lost bond prices fall and interest rates skyrocket. This can land countries in acute payment difficulties as soon as they have to replace maturing government bonds with new ones and possibly even have to seek additional credits. In this way, in a matter of weeks or even days a chain reaction can occur, threatening to bring down the entire euro-construction. This drama was played out in front of an astonished global audience from early 2010.

In defence of Angela Merkel, it can be pointed out that the ‘SHT’ is not her invention, but was built into the foundations of the monetary union in the early 1990s in the form of the ‘Maastricht criteria’. The euro zone, like the single market, is conceived as a union of states that compete with

one another as if they were enterprises (Troost and Hersel 2012).³ This construction has already proved highly problematic for the single market – for example, because in the rules in accordance with which competition takes place social standards do not have anything like the importance of the free movement of capital – but for the Monetary Union it amounts to a knock-out clause: without, among other things, a common tax system, equalisation payments between economically stronger and weaker regions or a common economic policy – in short: without central state institutions that previous economic history had shown to be indispensable conditions of a monetary union – it can be assumed that the existing differences in terms of economic performance between the participating states will only increase rather than diminish, so much so that the construction of a ‘competition union’ between an export and surplus oriented core and a periphery dependent to a considerable extent on imports financed by external credit has unleashed a dynamic of increasing imbalances within the EU (Horn *et al.* 2009).

However, it was more than ten years before it occurred to decision-makers that there was a problem, because Greece’s economic growth was always above the euro-zone average. The illusion was dispelled in 2008. The faulty design of the competition union could not withstand the storm of the international financial and economic crisis. In order to avoid its collapsing like a house of cards several rescue packages were deployed on a trial and error basis – or rather ‘error and trial and another error’ – and finally the European Stability Mechanism (ESM) was created.

However, this did not calm the situation. The European Central Bank (ECB) overcame its misgivings – to be more precise, the misgivings of the Bundesbank – at the end of 2011 and provided the banking sector with, in effect, unlimited credit at zero interest in order to boost lending to the crisis states at lower interest rates. Naturally, it would have been simpler to have provided the states concerned with central bank credits directly, but the ECB statutes do not allow it. The point of the diversion was concisely expressed by the then chief economist of Deutsche Bank: ‘By passing on cheap central bank money to states with a mark up the banks make profits from taxpayers. This attracts less attention

3. Just how peculiar the logic underlying this concept is becomes clear when one puts the simple question: what happens to the employees of an enterprise that is unable to keep up with the competition and disappears from the market? The reader is no doubt perfectly capable of following this line of argument and transposing it to states.

than when taxpayers' money is applied directly in order to rehabilitate bank balance sheets' (Mayer 2012). When even this failed to calm things ECB President Mario Draghi declared in July 2012 that the ECB would, if necessary, itself intervene in the markets and buy up government bonds to an unlimited extent in order to bring down interest rates for the endangered states. The announcement alone did the trick: the situation steadied and the interest rates of the crisis states fell substantially.⁴

Naturally, the rescue path on which the ECB set out in 2012 is inconsistent, first, because, as part of the Troika, the ECB at the same time compels the endangered states to take medicine that only makes the illness worse. And second, it is undemocratic because in the extreme case the unelected ECB executive board can decide which bonds are to be purchased without limit and which are not – in other words, whether states that are unwilling to kowtow to the Troika's diktat are to be left to the mercy of 'the markets', while obedient crisis states can be protected with a firewall. Whatever the case may be without this ECB intervention the euro zone would probably already have broken up.

Although the powers-that-be in Berlin and Brussels were not enthusiastic about these activities on the part of the ECB they quickly realised that 'the Greek crisis was a godsend for anti-Keynesians' (Krugman 2013: 6). They launched a 'silent revolution' that, as former Commission President Barroso put it, 'will lead to a quantum leap of economic surveillance in Europe' (EUobserver 2011). In this way, step by step – or 'error by error' – the madness found its method.

3. The 'austeritarian' regime

German Chancellor Merkel, in a speech at the global economic forum in Davos, summed up the two main aims of this 'silent revolution' as follows: 'We in Europe intend ... to develop our economic and monetary union into a real stability union. This is anything but a quick-fix

4. The pragmatism of the ECB induced the most devout believers to go before the German Constitutional Court. Its first judgment in this matter in February 2014 in essence calls 'the whole existence of the monetary union into question', in the opinion of one of the authors of the present book (Watt 2014a), who further notes that, fortunately, 'the markets' have thus far not taken this new threat seriously. But since the proceedings have not yet been concluded the time bomb continues to tick away (on this see also the contribution by Annamaria Simonazzi in this volume).

emergency operation. It's a strategy for the long term – a strategy that combines structural reforms designed to enhance competitiveness with the consolidation of public finances.' In a series of decisions by the EU institutions ('fiscal compact', 'sixpack', 'twopack' and so on) what will be practiced as 'new economic governance' within the framework of the 'European semester' took shape. Leschke, Theodoropoulou and Watt in their contribution to this volume describe the basic structure of this set of instruments and analyse some of the main results of its implementation, while Schulten and Müller show what this means for employees and trade union rights. A few highlights will suffice here that are particularly important for a better understanding of the links between EU policy and developments in particular countries.

The first and predominant focus of 'economic surveillance' is the 'consolidation of public finances'. This is accomplished primarily with the help of spending cuts; the revenue side, by contrast, receives little attention, with the exception of (regressive) consumption taxes. Austerity measures tend to be focused on health care, social services, pensions and infrastructural investment (OECD 2012: 41, 52ff). In the following country chapters the consequences of this approach are vividly described.

The focus on budget consolidation, primarily by means of spending cuts – so-called 'austerity policy' – is notable because the sequence of events is evident: first came the crisis, then public debt rose rapidly (see Figure 2). The latter was primarily the result not of the stimulus packages and rising social expenditure, as had been usual in previous crises, but of the bailout of the private banking sector. By way of example, in Germany public debt in relation to GDP rose from around 60 per cent to over 80 per cent, overwhelmingly because of the bank bailouts (BMF 2012).

By a quite breathtaking sleight of hand the effect was declared to be the cause and the victim the perpetrator. The rehabilitation of public budgets has been taken by the leading actors in Brussels, Berlin and elsewhere to be self-evidently the key to everything: in the short term debt reduction is to serve as defence against speculative attacks on the government bonds of 'debt sinners'; in the medium term it will furnish the 'confidence' needed for economic recovery; and in the long term it is the only way of protecting our 'children and grandchildren' from having to bear the costs arising because today 'we are living beyond our means'. There is no need to search for an elaborated rationale behind this approach, any more than in the case of the 'Swabian housewife theorem'

mentioned above. Over the past thirty years neoliberal doctrine has become strongly established as an interpretative framework independent of time and place. Such a thing cannot be thrown overboard in a matter of months. Especially not when 95 per cent of journalists strongly believe that 99 per cent of 'economic experts' cannot be wrong (the figures relate to Germany, where this piety is at an extremely high level by international comparison – matched only by the Directorate General for Economic and Financial Affairs in Brussels).

Austerity policy in combination with so-called 'internal devaluation' is the hard core of EU crisis policy. Leschke, Theodoropoulou and Watt (Chapter 13) describe the scope of the so-called 'scoreboard' with which the European Commission monitors the economic development of the member states. At its centre are budgetary policy and 'structural reforms for more competitiveness'. 'Social policies, in the broadest sense, have today been designated and targeted as the EMU's main adjustment variables' (Pochet and Degryse 2012: 217). For the cheerleaders of EU crisis policy, labour costs are the decisive factor in prosperity or otherwise. Schulten and Müller show with what insistence the universal remedy for boosting price competitiveness stemming from the 1980s and 1990s has been pursued, and in the relevant country chapters it becomes clear what the effects of this policy have been in a relatively short time.

The basic principle of neoliberal 'structural reforms' is 'one size fits all'. One is reminded of Joseph Stiglitz's (2002: 64) anecdote about how in the IMF's conditions applying to the granting of credits to countries stricken by financial crises in the 1990s someone once forgot to replace the name of the respective country using 'copy and paste'. The countries with which the Troika has concluded 'agreements' have been prescribed a programme of cuts and deregulation which is described by Maria Karamessini in her chapter on Greece as an 'acceleration of the neoliberal project'. The rescue packages provide an opportunity, at least in some EU countries, to implement an 'austeritarian' (austerity imposed in an authoritarian manner) regime (Dufresne/Pernot 2013: 4). The German government has played a decisive role in implementing this regime.⁵

5. Jürgen Habermas (2014: 88) has summed up this role by saying that the German government has played on Germany's 'semi-hegemonic status' in Europe 'quite robustly' and has compelled the 'crisis countries to implement far-reaching "reforms", without discernibly taking pan-European responsibility for the severe consequences of this socially one-sided austerity policy.'

But how can ‘structural reforms’ be implemented in countries where the writ of the Troika does not run? The idea is to agree on so-called ‘competitiveness pacts’ to strengthen the ongoing ‘authoritarian constitutionalisation’ (Oberndörfer 2013). While critics regard this as contrary to European law, with the fiscal pact ‘Pandora’s box [has already been] opened’ in this regard (Oberndörfer 2013: 84). The establishment of such ‘competitiveness pacts’ has not proved easy, however. ‘Only Merkel still wants economic reforms’, ran the headline in FAZ on 21 December 2013, which reported that, in the Chancellor’s opinion, ‘reform fatigue’ was rampant in most member states because ‘the pressure from the financial markets and thus pressure for reform had abated’. Furthermore, in some states – such as the Netherlands – the flame of solidarity has dimmed. But the euro states must not leave things, she warned, until ‘the markets show us the red light’. It is as well to be reminded occasionally who has the final say and sets the lights to red or green.

But let’s now turn to the effects of the reforms that are alleged to have moved the markets to switch the indicator light to amber.

4. Deepening the crisis with the efforts to fix it

First of all: what has the austeritarian regime done for growth? As can be seen in Figure 1, gross domestic product (GDP) has returned to or surpassed its pre-crisis level in only four of the countries analysed in this volume. In the countries on the so-called periphery it has fallen much more than the euro-zone average, most dramatically in Greece, where austerity has been applied most severely. On average, austerity policy has driven euro-zone countries into a deepening recession.

This correlation has recently been rather soberly confirmed by the IMF on several occasions. The economists of the IMF even felt obliged to re-examine the consequences of all short-term consolidation programmes implemented across the world over the past 30 years at the IMF’s instigation. The outcome was that during a period of five years GDP has fallen substantially, unemployment – in particular long-term unemployment – has risen, wages have fallen and inequality of income has increased (Batini *et al.* 2012; Blanchard and Leigh 2013).⁶

6. Nevertheless, within the framework of the Troika the IMF continues to help implement policies that its own economists regard as mistaken. However, tensions within the Troika appear to be increasing.

Figure 1a Change in GDP in selected EU countries below the euro-zone average (EA-18) (2007 = 100)

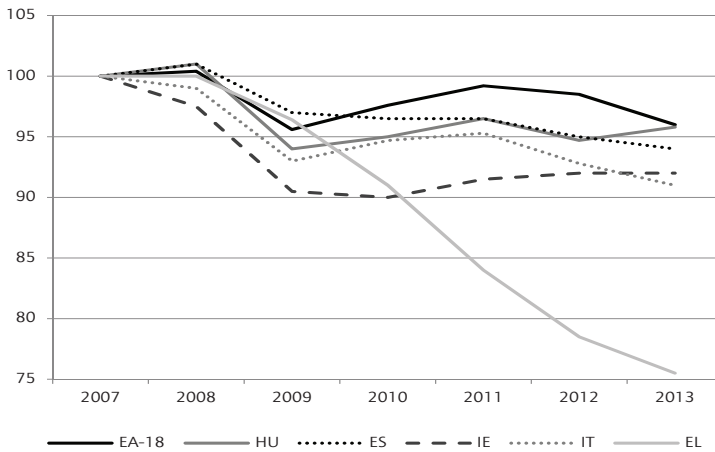
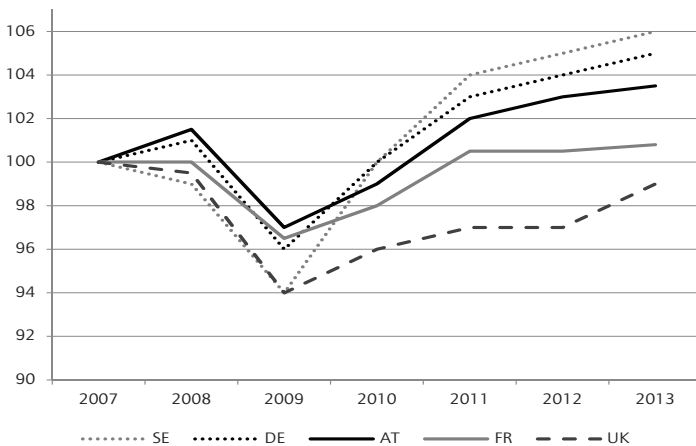


Figure 1b Change in GDP in selected EU countries above the euro-zone average (2007 = 100)



Note: For EU country codes see annex of the book.

Source: Eurostat; author's own compilation.

Needless to say, due to the prolonged and deepened recession in most countries unemployment is rising (on this see the chapter by Leschke *et al.*). Financial Times columnist Martin Wolf (2013a) puts it in a nutshell: ‘Austerity has failed. (...) Austerity cannot kill the economy. But it can inflict a great deal of unnecessary suffering and waste. Austerity is a treatment that aggravates the illness.’

Ironically, this policy has failed to achieve even the indirect goal of lowering public debt in relation to GDP (De Grauwe/Ji 2013). Because cuts in government spending reduce GDP even faster than state budgets the government debt ratio has risen (Figure 2).

The obsession with combating the crisis by reducing public debt has triggered a particularly calamitous negative spiral because austerity policy – as emphasised by the IMF economists – has negative effects on distribution. Increasing income inequality was among the major structural changes in most EU countries in the two or three decades preceding the crisis (OECD 2011; Ballarino *et al.* 2012). Critical analyses have presented this as one of the main causes of the global financial crisis, because increasing profits and capital income – encouraged by financial market deregulation – sometimes accompanied by higher private debt and long-term falling economic growth rates were increasingly re-invested in speculative investment classes (Hufschmid 2002; Foster and Magdoff 2009). The 2008/2009 crisis gave further impetus to this trend in most countries, after a brief profit plunge (OECD 2013). To make matters worse, austerity policy has only exacerbated the basic problem. Paul Krugman (2013: 13) sums it up nicely: ‘while economic policy since the financial crisis looks like a dismal failure by most measures, it hasn’t been so bad for the wealthy. Profits have recovered strongly even as unprecedented long-term unemployment persists; stock indices on both sides of the Atlantic have rebounded to pre-crisis highs even as median income languishes. It might be too much to say that those in the top 1 percent actually benefit from a continuing depression, but they certainly aren’t feeling much pain, and that probably has something to do with policymakers’ willingness to stay the austerity course.’

Wolfgang Streeck (2013) sees in this policy, which continues to flourish in Europe more than anywhere else in the world, as the latest culmination of a historical development from the ‘tax state’ through the ‘debt state’ to the ‘consolidation state’, in terms of which he demonstrates the tension between capitalism and democracy. He convincingly analyses

Figure 2a Changes in government debt in relation to GDP in selected EU countries: countries making severe spending cuts since 2009*

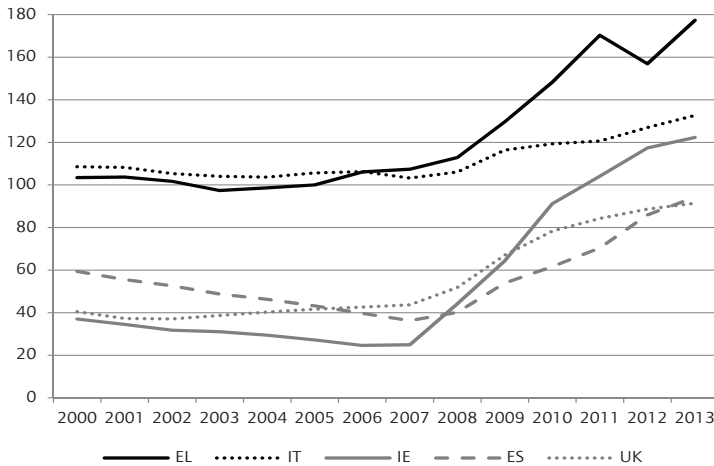
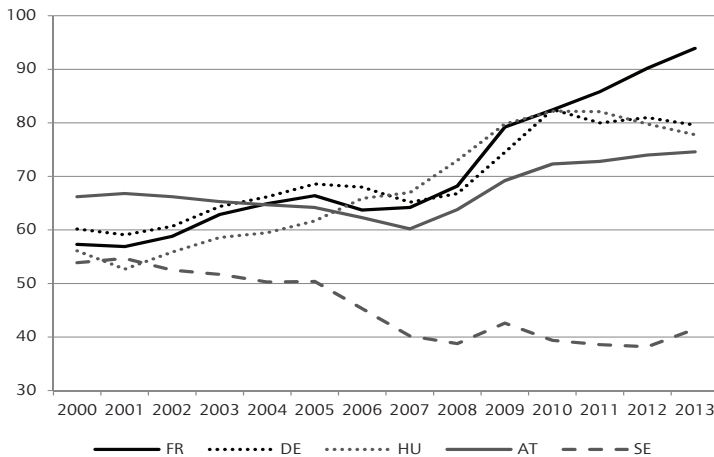


Figure 2b Changes in government debt in relation to GDP in selected EU countries: countries making less severe or only modest spending cuts since 2009*



Notes: For EU country codes see annex of the book.

* see OECD 2012 and de Grauwe/Ji 2013

Source: Eurostat; author's own calculations.

the financial crisis and European crisis policy as the current expression of a problem that has been around for over 100 years, namely that the modern state has found it more and more difficult to obtain the resources it needs to perform its increasing tasks from a 'society of private property owners': 'The cause of public debt is not too high spending but too low revenues' (Streeck 2013: 8).

The following chapters on the countries hit hardest by the crisis and by the measures taken to combat it since 2010 show strikingly how current austerity policy constitutes a second blow to lower income groups and with even greater force, while upper income groups remain largely unaffected. As observed by Leschke *et al.* (in this volume) the fact that social spending has been cut most savagely in just those EU countries in which the poverty rate was already highest is lamentable.

The key to current developments can be discerned in the fact that rising public debt, which has provided an excuse for austerity policy, is largely due to the bailout of the banks. In days gone by, so much capital was annihilated in capitalist crises that the remaining capital could be invested profitably again. This economic 'purging function' of crises has to a considerable extent been blocked since 2008 by the 'nationalisation' of private debts (Deppe 2013: 38ff). Although there have certainly been considerable losses, the profitability of a large part of surplus (some might say 'superfluous') capital has been maintained for the time being using taxpayers' money. In other words, rising inequality prepared the ground for the great crisis and austerity policy has served to sustain the threat. The victims are thus being persecuted instead of the perpetrators, who – so far, at least – have emerged from the crisis stronger than ever. What does this portend for the economic recovery that is purported to have set in at the end of 2013? Does it not show that the drastic remedies are finally beginning to work? Naturally, critics of EU policy incline to the view that the perceived signs of recovery are modest, to say the least. I don't want to yield to this temptation – although such fears are well founded – but rather to draw attention to another problem. If only due to the need for replacement investments, any crisis – as long as capitalism and cyclical crises continue to exist – has to bottom out at some point. What we have seen in recent years, however, has been a prolonging of the agony by means of the EU's efforts to get to grips with the crisis, making matters even worse. In practice, this means that unemployment, poverty and the dismantling of social protection have been pushed so hard that the economic data have improved almost by de-

fault. To take the example of Spain, due to social immiseration demand for imported goods has receded, while at the same time the sharp fall in wages has given a quasi-automatic boost to Spanish industry's price competitiveness. This turnaround from a chronic current account deficit to a modest export surplus has enabled the cheerleaders of 'reform' to boast of its success. In simple terms what we are seeing in some European countries today is recovery by virtue of impoverishment. It is important to understand, however, that this will inevitably leave its mark *over the long term*, indeed for decades to come. Crop destruction can be accomplished in a matter of minutes; recultivation takes considerable time. This is because the most important basis of any economy – human productive capacities – have been debased and neglected.

In this way the 'purging function' of crises is stifled in a more far-reaching sense. In contrast to earlier major crises the current one has not, to date, given rise to any innovation – in the good sense – in respect of either the economic development of individual countries or their social and environmental reorientation. And when it comes to a 'transformation project' like the one undertaken in the United States in the 1930s, which paved the way for the social harnessing of post-War capitalism the less said the better (Deppe 2013: 50). To be sure, the conditions for – and challenges facing – such a transformation are entirely different from those in the middle of the last century and would also entail, due to lower growth rates, much bitterer conflicts about distribution (Klein 2013: 47). To sum up, much ground has been lost in the current crisis but there has been no innovation in terms of socio-economic development.

This applies not only to the countries hit hardest and most dramatically by the crisis. This is shown clearly by the variegated picture provided by the country analyses in this volume, with all its contrasts, contradictions and paradoxes.

5. Continental drift

The first overall impression that emerges from the ten country chapters is that of a continent drifting apart. If one considers the trends in context it becomes clear how much the obsession with cutting public spending and shrinking wage costs – the pivot of the new economic policy governance in the EU – is blocking the urgent reorientation of socio-economic models in the member states.

This observation is important because criticisms of the ‘structural reforms’ driven forward by the austeritarian regime should not give rise to the conclusion that – particularly in the most crisis-ridden countries – there is no need for reform. On the contrary, as the following country analyses show, every country is afflicted in its own special way, thereby making it vulnerable to crisis. The universal remedy being prescribed to these countries – now that ‘the party’s over’, as James Wickham put it in the case of Ireland – bears no relation whatever to the nature of the illness. It will at best retard any recovery.

The stubborn adherence to questionable or even manifestly bankrupt growth models is most striking in the places hit hardest by the crisis. We should thus look at these countries first.

5.1 Pathogenic medicine

After the initial phase of the crisis – namely the global financial and economic crisis of 2008/2009 – *Greece* has suffered the most dramatic slump of all the euro-zone countries. Maria Karamessini depicts the ‘punitive character’ of financial assistance and the consequences of ‘shock therapy’ for her country, which has ‘unleashed a spiral of austerity – recession – austerity’. She describes, on one hand, the social devastation that has ensued, which will continue to afflict the country for a long time to come. On the other hand, she emphasises the lack of economic prospects due to this approach: austerity and privatisations deprive the state of the tools with which it might be able to foster growth. ‘Growth will thus entirely depend on incentives to foreign multinational capital and the most internationalized fractions of Greek capital. The greatest incentive will be an impoverished working class deprived of its rights and a great labour reserve created by mass unemployment.’

In contrast to *Greece*, *Italy* has a major tradition of internationally competitive industrial production, ranging from the garment industry to mechanical engineering. However, crisis has been creeping up on Italian industry – which moreover hardly expanded into the southern part of the country – since long before 2008. Annamaria Simonazzi takes a somewhat more optimistic view of the endogenous potential of the Italian economy than many other experts from that country, but she takes especially the state and the political system to task. She explains ‘Italy’s vicissitudes’ among other things in terms of an interaction of tax evasion,

tax elusion and tax cuts, which, along with an inefficient and clientistic public administration, substantially impedes expansion of infrastructure and, especially, social services. Tax policies have opened a 'perverse channel of income redistribution', as 'the middle classes (and the 'third Italy' in the north-east and elsewhere) managed to avoid paying taxes and turned their tax notices into bonds, underwriting the loans required to finance the deficit'. Other factors include the policy of labour market deregulation aimed at bringing about – inadequate in her opinion, too – flexibility by means of social insecurity; the lack of any kind of industrial policy; and 'a political stalemate making bold reforms to clean out cronyism and corruption almost impossible'. Against this background she explains the situation that in Italy the recession has snowballed into a bigger and prolonged burden for the Italian economy and society. She sees no light at the end of the tunnel.

Stagnation, by contrast, is the last thing that comes to mind in relation to *Spain*. In fact, in the past 30 years this country, in contrast with the rest of southern Europe, has experienced the most rapid capitalist modernisation process. Josep Banyuls and Albert Recio describe an economic and social dynamic shaped by the 'contradictory attempt to apply neoliberal policies in a society that was trying to develop a – previously non-existent – welfare state'.⁷ The economic boom was increasingly sustained by a construction and speculative bubble nourished by foreign debt. The bursting of this bubble is now being exploited as an opportunity to impose a 'neoliberal-conservative project' involving privatisation in health care and education, the dismantling of social services and rights, but also the strengthening of conservative-elite elements. Thus in a major education reform more mechanisms of social selection were introduced; the financial basis of the state school system was weakened; and civic instruction reduced in favour of Catholic religious instruction. Social and regional inequalities are likewise deepening. As a consequence, 'the need of the family to be the provider of welfare services returns even stronger, in a context in which the public sector is no longer providing basic services.' This policy is driving the country towards 'a falling back to the old Mediterranean model, as many of the cuts are aimed at burdening families, or rather the women with managing to fill the gaps caused by the

7. One striking indicator is the enormous increase in female employment: on the eve of the crisis the employment rate among women, according to Eurostat figures, was 55 per cent, having been only 40 per cent in 2000 and 30 per cent in 1990. By comparison, the EU27 average was around 59 per cent in 2008 (50 per cent in the EU15 in 1990), in contrast to 47 per cent in Italy and 49 per cent in Greece.

lack of public provisions.’ In the economic domain Banyuls and Recio also consider the ‘structural reforms’ to be backward-looking: instead of promoting scientific and technological advance, opening up to more productive and cooperative production methods or eliminating barriers to social mobility, the government programme ‘reinforces an obsolete production model based on low wages and precarious employment, limiting the possibility of change and reproducing all of the problems which have traditionally affected the Spanish economy.’⁸ It is exactly the production model that initially enabled Spain to achieve high growth rates until it came under pressure from central and east European enlargement and was partly replaced by the real estate boom of the 2000s as a new growth engine. Thus, Spain is being driven ‘closer to the experience of many Latin American societies affected by adjustment plans rather than the Central European model that it has spent years trying to emulate.’

As in Spain, in *Ireland*, too, a real estate boom financed by private debt ushered in the crisis. Growth was so rapid that this traditional emigrant country turned temporarily into an immigrant country. When the bubble burst the government debt ratio exploded from around 25 per cent on the eve of the crisis to almost 120 per cent five years later, primarily as a result of the unprecedented assumption of all the debts of the banking sector, which had been heavily involved in speculative trading.⁹ Among the countries whose budgets were taken under the umbrella of European rescue efforts Ireland’s development is the one held up by the European Commission as an encouragement to others. James Wickham in his analysis examines the contradictions and shortcomings of this success story. The main growth engine, alongside the banking sector, comprises foreign – especially US – direct investments. Ireland’s attractiveness in this respect lies in large measure in its low corporate taxation, favoured by, among others, large software and internet firms for their global businesses. Wickham finds it ‘bizarre’ that the entire party spectrum has ‘made [the low corporate tax rate] into a symbol of national independence’, which has to be defended against the criticisms of other EU member states: ‘Far from stimulating any re-think of the national development strategy, the crisis turned the reliance on FDI into a national fetish’.

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8. Steinko (2013: 148) illustrates the economic strategy being pursued in Spain at that time with a quote from a minister for economic affairs from 1990: ‘the best industrial policy’ is one ‘that doesn’t exist’.
 9. In the meantime, ‘the dangerous shadow banks in Ireland are flourishing again’, as FAZ (1.3.2014) reported with some concern, and are handling an estimated 70 per cent of the country’s financial transactions.

The Irish growth model is not only a striking example of the increasing predominance of national egoism in the EU as a result of the crisis – other examples are the defence of the City of London against the financial transaction tax by the British government and the defence of the German automobile industry against strict CO₂ directives by the German government). It also shows how great the obstacles are to developing a coordinated economic and tax policy, which is essential for a functioning monetary union, but also how comparatively easy it is for the participating governments to reach agreement on cutting social spending and deregulating labour markets as a recipe for boosting competitiveness.

5.2 You don't need the Troika to wreak havoc

The four countries we have used so far to exemplify adherence to unsustainable or even manifestly bankrupt growth models are members of the euro zone. The structure of this monetary union has served only to exacerbate the problems, but also in countries without the euro revision of previous growth models is being undermined, even if it is accompanied, as in *Hungary*, by anti-neoliberal rhetoric.

András Tóth describes Hungary's socio-economic development under the reign of charismatic right-wing populist prime minister Viktor Orbán as a 'selective economic nationalism'. The previous model, as in Ireland, was reliant on foreign direct investment. To some extent, this was the other side of the coin of the Spanish growth model that faltered in the 1990s because German industrial companies in particular diverted their supplier and investment strategy from southern Europe and France to the new member states (Duval 2013). However, the new industrial engines in Hungary have long since ceased to provide the rest of the economy with much impetus. Rapidly increasing private and public debt in the years before the crisis yielded short-term growth, but did nothing about the fundamental problem. This model collapsed with the advent of the crisis and under pressure from the European Commission the – then still social-liberal – government switched to austerity. The widespread disenchantment to which this gave rise enabled Orbán, similar to Rajoy in Spain, to swing the pendulum to the right. He established a regime sustained by an absolute majority (sufficient to enable it to change the Constitution) with strong echoes of national chauvinism, racism and anti-Semitism, which was returned to power at the parliamentary elections in April 2014. Orbán's policies are, on one hand, neoliberally inclined, as

indicated by the labour market ‘reforms’, massive social spending cuts and restrictions of trade union rights, as well as the continued efforts to attract foreign investors. On the other hand, this is combined with the systematic promotion of and preference given to influential domestic suppliers in the home market and in the case of public contracts. Furthermore, the highly indebted segments of the middle and upper classes (economically speaking) were given the chance to settle their debts with foreign banks at one fell swoop at a very favourable exchange rate, very much to the chagrin of, in particular, Austrian credit institutions. All of this has repeatedly brought the European Commission into the arena, but even legal measures are only grist to the mill of nationalist rhetoric. Tóth warns that other, larger countries could follow Hungary’s right-wing populist example. In the short term this mixture of neoliberalism and reactionary nationalism can be relatively successful, but the fundamental economic problems are not being addressed and the effects on social standards and the political culture are, in Tóth’s view, devastating.

While legal development in Hungary was at least partly triggered (if not caused) by intervention by Brussels what is perhaps the most massive austerity steamroller in Europe was set in motion without any help or even compulsion from Brussels or Berlin. This is shown by Damian Grimshaw and Jill Rubery on the example of the *United Kingdom*. In the wake of a number of social adjustments to Thatcherism – such as the statutory minimum wage and the significant expansion of public services – made by the New Labour government the current government is pursuing a radical and broad-based austerity policy in public services and social spending, combined with a new privatisation wave that for the first time has its sights on the health service. Grimshaw and Rubery consider this to be a fundamental restructuring of the United Kingdom towards a ‘true neoliberal employment and social model’ with a ‘shrinking [of the] public realm’ that is part of neoliberalism’s very core. Even a, by some measures, growing economy – after years in the doldrums due to austerity – does nothing to change either the basic problems of the British economy or the weak productivity growth, low investment and a current account deficit stretching back 30 years. The economy also remains unduly dependent on the financial sector (see also Wolf 2013b). To make matters worse, as in Spain, the ever deepening social and regional divisions will continue to exert their baleful influence for many years to come. Grimshaw and Rubery conclude that ‘the UK is likely to witness a “lost decade” of stalled economic output and investment, falling real wages, growing debt and a resurgence of unsustainable asset bubbles.’

The example of the United Kingdom shows even more clearly than that of Hungary that it would be one-sided and delusive to understand the austerity regimes established in a series of EU states as due primarily to the dictates of the Troika or pressure from Brussels (and Berlin). To be sure, this pressure is massive, but it is based on fundamental decisions taken by all heads of state and government and the numerous national parliaments which, for example, approved the 'Fiscal Compact' and in some cases even conferred constitutional status on it. There can also be no doubt that the official designation of Troika directives as 'memoranda of understanding' represents a ridiculous attempt at misdirection to cover up the real balance of power. This applies especially to developments in Greece and Spain, however much their national elites have endorsed and actively been involved in this policy and however much they represent their own direct interests. To drive this point home, with reference to Spain: the roots of the current government party reach back into the Franco era and are based on a clerical-reactionary tendency still existing in Spanish society. However, this tendency – not least against the background of capitalist modernisation in recent decades – has long been too weak to create the basis required for such a socially, politically and economically reactionary government policy on its own account. This is where Brussels and Berlin come in, offering the Spanish government a welcome excuse to declare that 'there is no alternative' and to generate such a degree of discouragement that a large part of Spanish society have come to feel that they must, at least for the time being, bow to the superiority of the powers-that-be, both domestic and foreign. The Spanish government's repeated claims that this foreign interference is an imposition can even be accepted as sincere, exhibiting the pride of these nationalist elites, embattled on all sides by corruption. Even though a domestic programme cannot be implemented without foreign help that does not mean that those providing the help have to be loved.

This complex situation opens the doors to right-wing populism – as in Hungary or France – and, on the other hand, makes it difficult for the opposition in many EU countries to offer a realistic prospect of bringing about a change of course in their own country. Another hindrance is the fact that the elites of economically stronger countries do everything in their power to divert attention from the real reasons for their (relative) economic and social stability and recommend a remedy to other countries that they do not apply themselves.

5.3 The concealed sheet-anchor

If one looks at analyses emanating from countries that have weathered the 2008/2009 recession relatively well they seem to have one thing in common: the governments concerned took measures that – as Christoph Hermann and Jörg Flecker show on the example of *Austria* – ‘temporarily returned to Keynesian deficit-spending’. This includes – as in the case of Germany – both state spending programmes and a ‘revitalisation of Austrian social partnership’. The welfare state with its automatic stabilisers has proved to be a stability anchor of last resort.

What Dominique Anxo has to say about *Sweden*, although different in detail, is essentially the same: the stabilising mechanisms included additional central-government transfers to municipalities even beyond 2008/2009 in order to avoid job cuts in social services, as well as an increase in public investment in infrastructure, but also tax cuts and higher transfer payments for low-income households. As in previous crises the Swedish krone was also depreciated but ‘compared with previous economic downturns, Swedish economic growth over recent years has been driven less by increases in exports than by an increase in public and private consumption, due both to increases in disposable household income and the additional appropriations to local government’. Anxo recalls that ‘the Swedish tax burden remains among the highest in Europe in spite of some decline during the past decade’. This made it possible to keep public debt low and, at the same time, the level of social and other services high.

This is all the more remarkable because the conservative Swedish government – much more radical than the Grand Coalition in Austria – is one of the most enthusiastic advocates of neoliberal crisis policies in Europe. James Wickham in his chapter on Ireland draws attention to a comparable paradox, namely the ‘curious survival’ of the welfare state, which he contrasts with what has happened in Greece: ‘In official media and public discourse increasingly the crisis is blamed not on the excesses of Anglo-American casino-capitalism but on allegedly excessive state expenditure. This is a curious inversion of reality. In fact, the crisis has highlighted the state’s ability to protect citizens against the vicissitudes of the market. In Ireland it is precisely the maintenance of the “European” welfare state, weak and imperfect though it may be, that has actually prevented social collapse.’ Even though Ireland’s recovery is celebrated in Europe, this ‘dark side’ is, of course, passed over in silence. The welfare state is an extremely unwelcome anchor.

This partial divergence of policies on the ground from the doctrine purveyed to a credulous media and to other countries is a pattern perfected by the various Merkel governments: prescribing medicine to others that one does not take oneself. Or at least that one does not take *for now*, and certainly not in the dosage forced on others: in Sweden, for a number of years now – much more purposefully than in Austria – the government has been sawing away at crucial pillars of the social model: neoliberalism has not left these countries unscathed, either. However, the care with which this is being carried out contrasts markedly with the deregulatory zeal that reached its zenith in the Agenda years in Germany and now is being proclaimed as a model for Europe.

I go into these points in more detail in the chapter on *Germany*. Deregulation in the German labour market is not the reason why the economy and the labour market stood up surprisingly well to the dramatic downturn from 2008 and developed relatively stably from the second half of 2009. Rather before the crisis they tremendously accelerated the increase in imbalances within the monetary union and thus helped decisively to prepare the ground for the near-collapse of the euro from 2010 onwards. In 2008/2009, however, previously written-off core elements of the pre-Agenda social model were reactivated, in particular the preference for *internal* operational flexibility, made possible by a 'social partnership' sustained by more self-confident trade unions. On top of that came something that the rest of Europe had awaited in vain during the preceding period of buoyant economic growth: average wages began to rise, not least because the trade unions now received more public support for their wage policy. As a result, for the first time this century economic growth in Germany was sustained more by its domestic market than by the – still high – export surplus. In brief, the relatively stable development of Germany's economy and labour market is due primarily to the fact that in recent years the ill effects of the Agenda policy on the labour market have begun to be curbed.¹⁰

The fact that the contrary message disseminated by the German government and the media finds such broad resonance is related to the excep-

10. And once the recent reforms – such as the statutory minimum wage and a strengthening of the option of declaring collective agreements to be generally binding – are in fact implemented not only will the damage be curbed but the first corrective measures will be taken. This will have positive side-effects for Europe, even though certainly unintended because the EU portion of the coalition agreement promised to maintain the policy of the previous government (Watt 2014b).

tional international success of German industry, enhanced by its primarily product-based competitiveness. The fact that this has nothing to do with the Agenda policy, either, is shown by the analyses of Austria and Sweden. In those countries there has been no even remotely comparable labour market deregulation, but there, too, the basis for value creation of the national economy has proved relatively robust in recent years. Thus the depreciation of the Swedish krone, mentioned above, was able to boost industry only because this industry is internationally competitive 'despite' high social standards.

At the same time, however, the analyses of the economically strong countries draw attention to another thing they have in common: Germany, Austria and Sweden run the risk, in one way or another, of forfeiting their strengths. In Germany, it is primarily underinvestment in social services and public infrastructure, together with failures in education policy, with their detrimental effects on training, that are gradually undermining future economic success. Similarly Austria which, in the words of Hermann and Flecker, 'seems to be able to hold on to existing achievements, but fails to make the necessary investments to cope with future challenges, including long overdue investments in public infrastructures and research, as well as in a profound social and ecological modernisation.' And Dominique Anxo concludes his chapter on Sweden – after referring to the high unemployment and signs of unrest in urban districts with majority immigrant populations in summer 2013 – with an anxious prospect: 'if Sweden fails to re-establish the conditions for a return to full employment, in particular to reduce unemployment and increase employment rates for some of the abovementioned vulnerable groups, we cannot exclude a progressive decline of the Swedish model, its coherence and the robustness of its social cohesion.'

France already finds itself enmired in such a process. Here the inability, currently widespread in Europe, of economic and political elites to recognise the particular strengths and weaknesses of their respective economic and social models is becoming evident in an especially worrying fashion, hindering them from concentrating on overcoming weaknesses and developing their strengths free from ideological blinkers. Florence Jany-Catrice and Michel Lallement recall that France's economic development has for decades been sustained, through a number of crises, by a strong domestic market orientation – which until recently was made possible by continuous increases in average wages – and that France belongs, alongside Sweden, to the 'group of countries with the most robust

protection mechanisms' which 'undoubtedly did much to counteract the economic crisis of 2008'. However, the fact that French companies have this time not resorted to short-time working to anything like the same extent as their German counterparts and instead have cut jobs signals a change of direction, which is increasingly carrying over to the political level: cutting labour costs instead of boosting the value creation base. In only ten years the share of gross value added of manufacturing in French GDP has fallen by 5 percentage points to only 10 per cent (less than half the size of Germany). The critical economists cited by Jany-Catrice and Lallement explain this among other things by strategic neglect of product innovation, which also finds expression in the fact that while in 1992 R&D spending by corporations represented 45 per cent of dividends, by 2011 this had plummeted to 25 per cent. In Germany it is generally not recognised that financial market capitalism is stronger in France – as expressed, for example, in companies' stock market capitalisation – despite the number of state-owned companies and substantial residual 'statism'; because of its almost symbiotic relationship with various forms of elite organisation in the economy and the state administration it exerts an innovation-constricting influence.

The conflict concerning France's economic policy orientation – and possibly also that of Italy – is likely, in the near future, to play a key role in determining how serious the commitment is to the guidelines agreed in Brussels on boosting 'competitiveness'. The Hollande government has thus far obediently adhered to the dogma that labour costs have to be reduced in order to improve competitiveness, growth and employment. Disappointment with this lack of leadership has induced many of those who in 2012 showed that they wanted to abandon the 'Merkozy' approach to turn rightwards. Thus France is becoming a vivid example of the grain of truth in Chancellor Merkel's dictum that 'there is no alternative' to current crisis policy: for the time being, there are no powerful – that is, politically credible and feasible – alternatives.

6. All change in Europe emanates from the nation state

Notwithstanding the already cited prognosis of chief hardliners in the European Commission 'the worst' is not behind us. Even if the economy in the euro zone is growing again, in the longer term the scorched earth left by austerity policies will not easily be made good, which paves the way for the next crisis. At the same time, Europe remains locked into

boosting ‘competitiveness’ by institutionalised competition between states and the new economic policy governance, which in the current global economy and in the face of the environmental challenges does not promise a greener future. Even the political ‘crop damage’ is clearly discernible: ‘Europe’ is coming to be perceived by more and more people as rather a threat than a promise and democratic rights are progressively being curtailed. In the euro zone it can be seen most clearly how realistic Joseph Stiglitz’s (2013) pessimistic judgement is: ‘The euro was supposed to bring growth, prosperity, and a sense of unity to Europe. Instead, it has brought stagnation, instability, and divisiveness.’

This evaluation hones in on the core problem: the continent’s economic recovery hinges on the ‘confidence of investors’ or of ‘the markets’. If this does not automatically give rise to confidence among *ordinary people* an excuse lies readily to hand: social and economic problems are explained as *national* problems (see also Sauer 2013: 124).

To a certain extent that is indeed the case. Except that they are social conflicts *within* nation states and not *between* them. This is shown by the country analyses in this volume. The economic development models of a considerable number of European countries have not proved sustainable but now they are supposed to be revitalised despite increasing social inequality and weakening of labour market regulation and the welfare state. In the meantime, the governments of the economically stronger countries, with whom before the crisis the weaker countries had entered into a poisoned symbiosis, keep an eye on whether the rules of the austertarian regime are adhered to. But even for the stronger economies this regime is becoming a trap they laid for themselves, preventing them from dealing with their own problems. Thus the participants in this competition union are becoming a burden to one another. They are bound together primarily by problems and a common evil that none of them want to face: the increasing inequality which is proving to be a challenge that does not respect national borders and which states are finding it more and more difficult to cope with.

Because all the member states are now in the hole their governments – under the tutelage of the German government – dug for themselves, strapped in by intractable agreements under European law, the view is gaining ground among critics that progressive reform of EU legislation and the monetary union is not feasible in the foreseeable future. Any attempt to fend off the threat to social achievements registered especially

in the second half of the twentieth century within the framework of the nation state is possible, for the time being, only within this framework. Wolfgang Streeck (2013: 218, 223, 256) has expressed this resignation categorically, declaring that 'constructive opposition is impossible': 'At present opposition to the consolidation state cannot be much more than sand in the machinery of capitalist austerity and its associated discourse'. What is needed – if only as the 'second best solution', according to Streeck – is to use the historically established institutions and the 'residual democracy in the nation states' as 'a stumbling-block on the downhill slope into a single market state purged of democracy' (Streeck 2013: 163, 189, English edition).

Experience goes back a long way with a strategy limited to defending the achievements of the nation state. This strategy for obvious reasons is predominant in northern Europe and the trade unions in these countries concentrate on this task to such an extent that they often show little interest in European policy. They have certainly chalked up a number of successes in this way; nevertheless, their power resources are being reduced by inches and their influence is gradually waning (see also the chapter on Sweden). Comparable experiences bring Hans-Jürgen Urban, in his contribution to this volume, to the conclusion that trade unions' influence may best be exerted by building up what he calls a 'constructive veto power' in the sense that 'it is used not to conserve status-quo structures but to contribute towards the reconstruction of the socio-economic development model.' He regards this as a key challenge to the trade unions in the European crisis. In other words, coping with this challenge must commence with ideas or concrete reform projects on re-orientation of the socio-economic development model in one's *own* country. This is the basis needed for the implementation of re-orientation at European level, which must be guided by – as Urban calls it – a 'pro-European critique of Europe'. The widespread uncertainty concerning how this dual challenge can be dealt with he calls the European-policy 'strategic gap' of the trade unions.

The trade unions are far from being the only and sometimes not even the most active opposition functioning as a 'stumbling block' in relation to the dismantling of the achievements of nation states. Maria Karamessini, Josep Banyuls and Albert Recio, in their chapters on Greece and Spain, emphasise popular opposition – in which they themselves participate – to the crisis policy of their governments and the EU. We occasionally read in the newspapers that there has been another general strike

or big demonstration. But anyone who seeks out (for example, in trade union publications or websites such as www.troikawatch.net) reporting on the activities of social networks and protest movements will be impressed in both political and human terms by the extent of the courage and resistance: one might mention the self-organised clinics for the many people denied access to the public health care system in Greece, the broad-based civil disobedience against evictions in Spain or, again in Spain, the months-long demonstrations, petitions and strikes against the privatisation of six Madrid clinics, which led to a climbdown – for the time being – by the city council.

However, Banyuls and Recio also draw attention to the problem: ‘Although there are important social movements against government policies they focus on concrete aspects and there is no clear alternative to the austerity and liberal policies. Neither the opposition parties nor the trade unions offer substantial plans for new development paths. Because a credible political alternative to the neoliberal policy of cuts and labour market deregulation is lacking the latter can be presented as the only realistic answer to the crisis.’

But the political situation is rapidly changing in Spain, and even more so in Greece, as Maria Karamessini emphasises: the left majority is proposing ‘a growth strategy which allows for fiscal adjustment through an increase in taxable income and radical tax reform and makes use of primary fiscal surpluses and external financing (from the EU and other sources) for poverty alleviation and public investment.’ However, she also points out that such alternative approaches can be realised only if the crisis policy currently being pursued in the EU is halted and scope permitted for national reform programmes. Thus alternative approaches could be negotiated only at the EU level.

Italy, in contrast to Greece and Spain, is not under the strict supervision of the Troika or the European Commission and still has more economic potential. But Annamaria Simonazzi, too, regards the predominant EU policy approach as a barrier, rather than a lever, for desperately needed reforms: ‘An alternative policy must be based on the tenet that aggregate demand must increase in order to create new job opportunities, and public (physical and human) infrastructure needs to be part of it. The tax base must be more equally spread and service provision must improve. This calls for a solution to the quandary of public employment and bureaucratic inefficiency. The concept of taxes must be connected again

with the concept of services: people need to relearn that what they pay is for their health, education, child and elderly care. We need an industrial policy to identify the direction of development, guide investment, endeavour to ensure that the increase in demand does not leak out in imports and devise means to support the upgrading of value chains. New industrial relations and the revision of labour market deregulation are also needed, distinguishing between flexibility and insecurity. Indebted countries surely must do their homework, but we must reach an agreement on which “structural reforms” are most needed.’

Thus, the interlinkage between progressive reform agendas developed at national level and mutual support between countries at EU level is unavoidable today. The calling into question and erosion of the social achievements of post-War capitalism began long before the introduction of the euro. The regulations and institutions created within this framework have increased the pressure, but they did not create it. It should also not be forgotten that there has been no attempt in Europe since the very first years of Mitterrand governments in France to pave the way for an alternative to neoliberalism at the national level. Taking up the resigned proposal to confine oneself to throwing ‘sand in the machinery’ would mean, literally, exhausting one’s efforts to preserve earlier achievements. The only way out of the dilemma is forwards. The difference from previous decades is that this is becoming less and less possible within the framework of the nation state. If it was enough in the twentieth century to refer to globalisation to explain the extent of this challenge – and the rapidly abandoned attempt in France at the beginning of the 1980s justifies this – in Europe today rapid economic integration and the ever tightening bonds of authoritarian governance mean that there is no ignoring mutual dependence across national borders. Anyone seeking a response to this on the left must be realistic enough to accept that in Europe today the following two things go together: *at national level there must be massive pressure for the implementation of reform projects so that the unavoidable conflicts at European level can run their course and the current blockades be overcome, thereby making it possible to realise national reform projects.*

It may be objected that the European treaties prohibit this or that and in any case the political balance of power in the EU rules it out entirely. With regard to the treaties it is only partly true, because programmes such as the DGB proposal for a ‘Marshall Plan for Europe’ or the EuroMemorandum (2015) address in detail the implementation op-

tions within the framework of existing institutions. The same applies to the 'Programme for Employment' presented by the Italian trade union federation CGIL (CGIL 2013), which demonstrates the scope for reform within the framework of the nation state in Italy. However, it is certainly true that, for example, the Council decisions on monitoring national budgetary and economic policy are formally well anchored and difficult to overturn, to say nothing of even more far-reaching ambitions, such as a social charter that would have the same legal status in the EU as the economic freedoms. But anyone wanting progressive change must not restrict themselves to what is possible or not in existing institutions, but consider how a political dynamic can be unleashed that makes possible more than was previously considered feasible.¹¹ Only in this way can institutions be changed. Thus what is called for is to think less in terms of institutions and more in terms of political processes.

Crucial for political dynamics within the monetary union is the point expressed by Austrian economist Stephan Schulmeister (2013: 45): 'the creditor is only as strong as the debtor is weak'. In other words: decisive support for economic policy alternatives even within only one nation state, linked to the demand for (at least) a loosening of the fetters, deviating from the current decisions and principles of the European Council and the European Commission, would put the whole policy mainstream of the single market and the monetary union to the test. Depending on the capacity for conflict and alliance building of a government that stepped out of line in this way – and, up to a point, was able to push the limits of the principle of unanimity in the European Council – the other governments would be called upon to tackle this provocation. And depending on the extent of their concern about alarming 'the markets' and a possible domino effect in the monetary union they would have to ameliorate or correct their previous course, to a greater or lesser extent. However, progressive movements and trade unions in other countries would thus face a new situation. Hitherto, they are likely to have had the impression that they lived in different worlds. In the event of an obvi-

11. On the other hand, it would be unrealistic to believe that the pressure for reform within particular nation states could to some extent be skipped by means of institutional reforms at the level of the EU and the monetary union. Macroeconomic governance at the EU level that came into being via parliamentary democracy could follow neoliberal guidelines, in which case welfare state achievements at the national level could be dismantled with even greater 'legitimacy' than at present. Streeck worries that a left pursuing a constructive European policy could in this way play into neoliberal hands and on this point he is broadly right – except that building up reform pressure in individual nation states cannot simply be neglected.

ously *political* crisis – not one provoked by ‘the markets’ – their options for joining forces would be much improved. It would be easier for all critical forces to exercise *social* solidarity beyond national borders instead of *national* solidarity within one’s own country, which is the likely outcome of the ‘Swabian housewife theorem’.

An institutional structure like that of Maastricht, which gives the green light to neoliberal policies virtually across the board, while showing red or at best amber for social standards and for mutual support and convergence of national economies, cannot be reformed without tough conflicts, crises and schisms. The impetus for such an unavoidably grim reform process would come from countries in which the desire to end the austeritarian regime and for a national social, economic and environmental re-orientation would be so strong that conflict with Brussels, Berlin and other power centres would be inevitable. ‘Constructive opposition’ at the EU level will ultimately only be as effective as ‘constructive opposition’ for reforms in individual states. As things stand at the moment, it is difficult to imagine such impetus for Europe coming from Germany. One thing is certain, however: everything depends on how impetus from other countries is taken up in Germany, especially by trade unions and other progressive forces.

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A crisis inside the crisis: Spain under a conservative neoliberalism

Josep Banyuls and Albert Recio

1. Introduction

After a long period of growth, which started in 1994, the Spanish economy entered into a deep structural crisis in 2007. The discussion of the reasons for this situation and the requisite policy response has been intense, with wide variations of opinion. From the conventional point of view, the crisis is mainly a problem of ‘market disequilibrium’. Others believe that there are structural problems related mainly to the weakness of the structure of production. The eruption of the international financial crisis led to the end of a model centred on construction and tourism as its growth drivers, with no other activities looming on the horizon to replace them. The fall in production was reflected in the labour market in unprecedented unemployment rates and an increase in poverty and inequality that opened a social divide that will be difficult to close.

Besides the breakdown of the production system the state of the public sector must be added as a driver of the crisis, although its role has changed over the years. From 2008 to 2010 the policies implemented by the Social Democratic government focused on two basic objectives. One was to alleviate the problems of the financial system; the second was to mitigate the negative effects of recession with regard to job losses by increasing expenditure and employment in the public sector. But these mildly expansive measures were abandoned, and at the beginning of 2010 the period of austerity started, with the implementation of deep expenditure cuts. The new path sped up exponentially in 2012 with the advent of the conservative government. They implemented more austerity measures and a radical ‘reform’ programme, with the clear aim of dismantling the welfare state and the public sector, as well as dramatically transforming labour regulation.

Austerity not only reduces public services, but also closes the door to a new productive model. The spending cuts in education and in research and development, as well as the ending of local development policies are among the obstacles preventing the development of new productive sectors. It is hard to believe that new activities, which will create jobs in the future, can develop without the support of public policies. On the contrary, these reforms reinforce an obsolete production model based on low wages and precarious employment, limiting the possibility of change to a new productive model and reproducing all of the problems which have traditionally affected the Spanish economy.

Analysis of the measures implemented and their impact reveals their incapacity to resolve the structural weaknesses of the Spanish economy and the ways in which they have added new social and economic problems to the existing ones. For this reason we can speak about ‘a crisis inside a crisis’: the implemented measures reinforce inequality, competitiveness based on low wages and employment informality, as well as strengthening emphasis on the family as ‘welfare state provider’, thus making solutions to the current situation even more difficult. In this chapter we focus on these topics. First, we analyse the background of the current situation and the problems in the productive structure. We then go over public policies and how they are exacerbating the problems. In Section 4 we introduce the effects of the crisis on the labour market. Finally, in the Conclusions, we point out some lessons learned from the crisis and present some ideas about possible alternatives and future prospects.

2. A foreseeable crisis

Before the advent of the crisis, the Spanish economy appeared to be successful in many respects: it had experienced a decade of sustained growth in production output and employment, women were gradually being incorporated into the labour market and unemployment was going down (Table 1). However, when the analysis is taken deeper than these primary indicators, it becomes clear that the situation was more complex and, indeed, disturbing. This is why, against this backdrop of apparent prosperity, there were voices saying that, despite modernisation and temporary success, Spain’s growth model was extremely fragile (Banyuls *et al.* 2009; Banyuls and Recio 2012).

Table 1 Selected economic indicators, Spain, 2003–2013

	Real GDP growth rate-volume, % of change on previous year		Current + capital account (% GDP)	Government deficit/surplus (% GDP)		General government gross debt (% GDP)		Employment rate LFS (2nd quarter)		Unemployment rate LFS (2nd quarter)	
	Spain	Euro area		Spain	Euro area	Spain	Euro area	Spain	Euro area	Spain (1)	Euro area
2003	3.1	0.7	-2.5	-0.3	-3.1	48.8	69.1	60.1	62.6	11.3	9.0
2003	3.1	0.7	-2.5	-0.3	-3.1	48.8	69.1	60.1	62.6	11.3	9.0
2004	3.3	2.2	-4.2	-0.1	-2.9	46.3	69.6	61.1	62.8	11.1	9.3
2005	3.6	1.7	-6.5	1.3	-2.5	43.2	70.2	63.5	63.6	9.4	9.0
2006	4.1	3.3	-8.0	2.4	-1.3	39.7	68.5	65.0	64.6	8.6	8.3
2007	3.5	3.0	-9.6	2.0	-0.7	36.3	66.2	66.0	65.5	8.0	7.4
2008	0.9	0.4	-9.2	-4.5	-2.1	40.2	70.1	65.1	66.0	10.5	7.4
2009	-3.8	-4.4	-4.8	-11.1	-6.4	54.0	80.0	60.1	64.7	18.0	9.4
2010	-0.2	2.0	-3.9	-9.6	-6.2	61.7	85.5	58.9	64.2	20.2	10.0
2011	0.1	1.6	-3.3	-9.6	-4.2	70.5	87.4	58.7	64.5	21.0	9.8
2012	-1.6	-0.7	0.5	-10.6	-3.7	86.0	90.7	56.1	64.0	24.8	11.2

Note:(1) In 2005 there is a break in the series due to a methodological change.

Source: EUROSTAT, Banco de España, INE.

Some of the reasons for this instability were deeply rooted in the model of development of Spanish capitalism during the Franco era. It was largely a closed economy whose opening up since the late 1970s has been turbulent. Other aspects could be explained by the accumulation of contradictions in Spanish democracy (since 1977), notably the way in whether the internationalisation of the Spanish economy has come about and the contradictory attempt to apply neoliberal policies in a society that was trying to develop a – previously non-existent – welfare state. Other contradictions have arisen during the latest phase of rapid development (from 2004), bringing about an extremely risky situation. This is consistent with the wage share of national income. Between 2000 and 2010, apart from some upturns, the wage share declined slightly, from 50 per cent to 48 per cent. But this coincided with a significant increase in employment, a factor that, all other things being equal, is likely to cause a rise in the wage share in national income.

The first major source of problems is the production model, with interconnected weaknesses on various levels. One of them is low productivity, which has been decreasing for years. This is largely due to a production model in which the importance of labour-intensive sectors has increased. In times of economic growth (except for 1961 to 1974) increases in productivity in Spain have been lower than in the other EU15 countries (Fina 2001). In times of crisis, productivity has increased more than elsewhere in the EU15, but this is a passive increase due to the high job losses and not due to the incorporation of technology or improvements in production efficiency. These trends are structural but during the last expansive phase it was more visible, and the Spanish economy was one of the economies in which productivity increased least in the period 1995–2009 (Meager and Speckesser 2011).

Related to the production structure weakness are the balance of payments problems. The Spanish economy repeatedly experiences deficits in its external trade (Pérez *et al.* 2011), leading to endemic external debt and hindering job creation. This deficit reflects persistent low competitiveness, mainly in industry, but also disequilibrium associated with dependency on basic inputs (especially energy). This situation was aggravated after EU entry due to the persistence of moderate deindustrialisation. This can be explained by a combination of factors: the small and limited technological development of Spanish companies (making internationalisation difficult), the limited scale of local plants (which has justified their closure when supranational industrial groups have implemented reorganisation), specialisation in mid- and low-level production (more prone to relocation to countries with lower salaries) and foreign control over the main industrial groups.

Furthermore, large domestic capital owners (especially the financial sector) discarded their industrial interests and focused on the financial sector, public works and privatised public services (Recio 2010). Only tourism and some agricultural segments can be considered successful sectors of specialisation in the international arena, but they have not been sufficient to balance out the problems created in manufacturing. Until the beginning of the 1990s the imbalances were tackled with successive devaluations, but since euro entry this option has been unavailable and the latest phase of expansion has led to a growing deficit and increasing indebtedness.

The other major ‘failure’ of the system is the public sector. Historically, Spain has been a country with low taxes and a small welfare system.

Table 2 Employment by activity, Spain, 1994–2007

	1994	2007	% change
Total activities	12,207.6	20,476.9	67.7
Manufacturing	2,427.0	3,118.9	28.5
Construction	1,117.2	2,693.5	141.1
Wholesale and retail trade; repair of motor vehicles...	2,108.9	3,211.5	52.3
Hotels and restaurants	738.0	1,443.8	95.6
Transport, storage and communication	712.0	1,176.3	65.2
Financial intermedia-tion	329.5	509.3	54.6
Real estate, renting and business activities	633.0	2,054.0	224.5
Public administration and defence; compul-sory social security	789.6	1,241.3	57.2
Education	670.6	1,128.0	68.2
Human health and social work activities	616.0	1,221.0	98.2
Other community, social and personal service activities	433.7	842.1	94.2

Source: Authors' calculations from EPA. Annual averages.

The democratic transition led to substantial changes, with the introduction of a modern tax system and the extension of public services. However, this expansion has been limited by the country's lax mentality towards tax and great tolerance of the unofficial economy. Since the early 1990s, a series of tax cuts have been instituted that are at odds with the greater social demand for public health services, education and so on. This was partly linked to the competition between the two dominant parties in the political arena. In this case, the tug-of-war between revenue and spending gave rise to underdevelopment of the public sphere rather than financial deficits. This shortcoming in particular affects the household/family system that has to take on an enormous burden with few resources.

The phase of spectacular economic growth from 1994 to 2007 masked these problems instead of solving them and, to some extent, aggravated them. In terms of production, the engine of this growth was undoubtedly construction, above all in the residential sector but also public works. The impact of this industry on all economic activity was unquestionable (Bielsa and Duarte 2011). The nature of this activity, which cannot be relocated, extended its impact across the country, although tourist and urban areas experienced the biggest growth. The enormous building activity boosted employment and tax revenues, but one of its downsides was the explosion of mortgages taken out by households throughout the country.

At first, this led to a financial bubble and severe household indebtedness, not to mention a serious problem of access to housing for lower earners (especially young people). The financial sector played a crucial role in this, taking loans from abroad to transform them into loans to property developers and individual buyers (Naredo and Montiel 2011). This explains why Spain's external debt has been mainly private debt. Secondly, it has led to serious environmental degradation, accelerating some existing problems (desertification, energy dependence and so forth). Thirdly, as this is an activity in which government regulation plays a key role in classifying land (for development), this industry became the main agent responsible for the problems of political corruption, especially at local level. The building boom encouraged an economic mindset of short-term profit based more on property transactions than on the pursuit of technical efficiency, training and improved competitiveness (Lopez and Rodriguez 2011).

The growth of the property market also had a complex impact on public policies, which were contradictory. On the one hand, the policy of tax cuts was accelerated under both the conservative Partido Popular and the Socialist Party (reforms of income tax and corporation tax, elimination or reduction of taxes on inheritance and donations, and so on). In the short term, the buoyancy in the property market compensated for the loss of revenue due to tax cuts, but when the property market slumped, tax revenues plummeted. Moreover, with the Socialist Party back in power a new boost was given to the welfare policies that people demanded, not only in traditional matters such as education and health care, but in new areas, and especially in aid for housing and policies aimed at families and dependents. One particularly clear example of the increase in spending is found in the budgets in the autonomous regions to which management

of social spending had been transferred. Behind this increase there was both the need to improve the standards of public services and the demographic and social backdrop, which is discussed below.

The traditional Mediterranean family model is based partly on distinct gender roles that have enabled many reproductive needs to be covered by female household members (although there is increasing evidence that this activity is often combined by many working-class women with unofficial paid employment). This model has partly broken down (Miguélez and Recio 2010) due to the changes in Spanish society in recent years: an increase in education, especially for women, changes in consumption patterns (which make a single family income inadequate) and the increasing instability of the traditional family model (growth of the divorce rate and short-term informal relationships). In addition, the aging population is giving rise to new care needs that families alone are unable to sustain. All of this pressure has led to demands for new social policies to support families and the creation of new labour market demand for care workers which, due to families' financial constraints, has generated an 'unofficial market for carers' (Simonazzi 2009).

All this resulted in strong employment growth for years. This employment growth soon required the mobilisation of a large reserve workforce, however, which explains the intense immigration to Spain.¹ This immigration occurred alongside policies that were fairly lax as regards entry into the country, while labour law within Spain was very restrictive. The result was that at several stages during this process this reserve workforce found itself in a situation of illegality or outside the law, which in turn fostered the growth of unofficial employment. At least this wave of immigration made a quantifiable contribution that enabled companies to cover their labour needs without generating inflationary pressure on wages. It often contributed to a deterioration in working conditions, however,

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1. Employment growth has occurred while the labour force has been increasing, with the arrival of immigrants and higher female labour market participation. Despite the dramatic economic growth the unemployment rate in this period was still high compared with other European countries. This is due to several reasons, three of which are particularly significant. One is job quality. Most of the jobs created in this period are 'bad' jobs, and people that can avoid them continue to look for a better one, remaining unemployed in the meantime. Bad jobs have been taken mainly by immigrants. The second is the high level of flexibility of the Spanish labour market, with a high level of replacement due to the intensive use of fixed-term contracts. Many workers move frequently from employment to unemployment and back again. The third aspect is the fact that, despite the significant employment creation, in some activities (some industrial branches, agriculture) there has been slow and continuous employment destruction, and those affected have found it very difficult to find a new job.

particularly in sectors where unofficial labour is particularly prevalent (especially the care sector, but also outsourcing in construction or services). Population growth also helped to generate demand for increased public services, which also explains some of the policy responses.

The financial system has played a central role in developments. In the crisis of 1975–1985 the private banking system was restructured (with generous state support) and was subjected to stricter regulations with regard to reserves. As a result, in the current crisis they have not experienced problems of the same magnitude as in other countries. As an effect of these processes, the private banking system became more concentrated (now there are only two big banks, Santander and BBVA, instead of six, plus two medium-sized banks) and the whole sector has successfully protected itself against competition from foreign banks. The biggest two banks have engaged in internationalisation (mainly in Latin America and the United Kingdom), reducing their dependence on the domestic market. On the other hand, there is a large group of savings banks, usually with the participation of local governments, mainly geared towards local markets. Both groups based their expansion on massive resort to foreign credit. A large part of these funds, especially in the case of savings banks, was devoted to feeding the real estate and housing bubble. When the bubble collapsed, savings banks faced major problems. Now they have been transformed into private banks or have been nationalised. It is important to take into account the fact that the problems of Spanish banks were not induced by their foreign activities, as in other EU countries, but rather home-grown, due to the domestic housing credit bubble.

In summary, the background of economic developments before the recession partly contributed to the conditions that dictated how it subsequently progressed: it promoted an economic development model focused on the volatile building industry, mobilised a reserve workforce in a very precarious social situation and weakened the country's tax base in a setting calling for higher spending. The recession has been worldwide, but the Spanish economy had accumulated sufficient features of its own to explain the dramatic situation we are now seeing.

3. Public policies: The road to conservative neoliberalism

Since the beginning of the crisis public policy has undergone a major change. It was only during the first period of 2008–2010 that there was

a timid attempt at a Keynesian response, but in May 2010 Rodríguez Zapatero's Socialist government adopted a clear shift towards austerity and neoliberal reforms, which have intensified as the situation has worsened. Today it is evident that structural changes have been initiated that depart radically from the model implemented in the democratic transition (1977). In a broad sense reforms are especially noticeable in the labour market and welfare policies. They are considered, in many respects and by most people, to constitute a significant loss of social rights and signify a clear transfer of power to the financial elite.

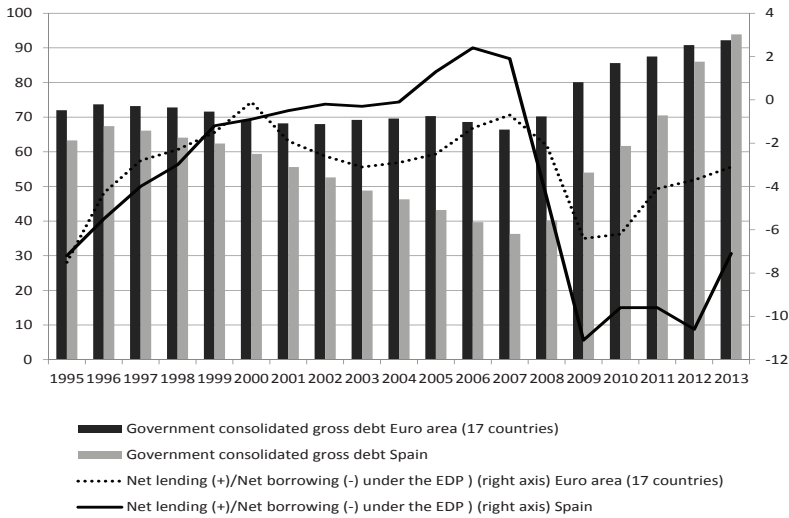
Transformations have been provoked by strong ruling groups who, in the crisis, have found a framework suitable for implementing their proposals. This framework is delimited by the problems generated by the crisis itself, particularly the dramatic rise in unemployment and the rising government debt (caused by the collapse in tax revenues), as well as the requirements and conditions imposed by the European Union, which are largely consistent with the interests of local elites or those that share the same political vision. Next we focus on the main changes that have taken place during the crisis.

3.1 The turnaround of 2010

At the beginning of the crisis the Spanish public sector had a low level of debt and a fiscal surplus (Figure 1), but in a short time this situation changed with the collapse of public revenues, which fell from 38 per cent to 31 per cent of GDP. This was due mainly to the high dependence of the Spanish economy and revenues on the construction and real estate markets. We must also reckon with the fact that since 1994, successive governments had implemented reforms and tax cuts and these have undermined tax collection. The aid to the financial sector, estimated at 20 per cent of GDP, has also helped to exacerbate the deficit.

To understand these changes it is necessary to consider additional political factors. On one hand, there was the electoral collapse of the Socialist Party, which enabled the conservative Partido Popular to achieve an overall majority in the general election and in the majority of the autonomous regions (Catalonia was an exception, won by the conservative-nationalist CiU party, which holds positions very similar to the Partido Popular in economic and social aspects). The electoral collapse of the socialists was prompted largely by their delay in recognising the importance of the crisis, their inability to control the financial sector and,

Figure 1 Government gross debt and deficit, Spain and EU17 (euro area)



Source: Eurostat.

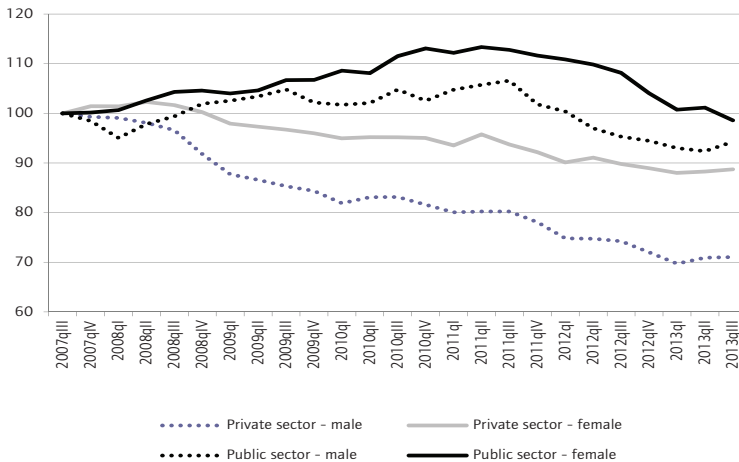
above all, the sudden change of policy and their uncritical acceptance of the dictates of the European Union and the IMF. In May 2010 the government adopted a drastic adjustment programme (reductions in public sector wages, pensions and public spending), followed by a labour reform, a pension reform, generous bailouts to the struggling banks and the introduction into the Constitution of an article that gives absolute priority in public spending to the payment of the public debt. This opened the doors for the victory of the Conservative party, giving it the capacity to control virtually every major resource of political power (government, parliament, autonomous regional governments, Constitutional Court). This accumulation of power has enabled the Conservatives to implement many of their most radical propositions without hesitation. On the other hand, we have the Spanish institutional model of territorial organisation, in which the management of most social policies (education, health care, social services, employment services and so on) depends on the Autonomous Communities. In the process of transferring the services responsibilities from the central government to the regional governments, however, more services have been transferred than economic resources. When public deficit problems have arisen, the central government has branded the regional governments as resource wasters

and has forced them to make significant budget cuts. Thus, the burden of adjustment has fallen disproportionately on social policies.

Overall, the changes can be summarized in three main areas. First, crucial cuts in public spending that have directly affected almost all welfare policies: education, health care, social services, active employment policies, culture and scientific development and research policies. These cuts have led to both a reduction of public employment (Figure 2) and a clear deterioration in living standards.

Secondly, the implementation of many of these ‘retrenchment’ policies has entailed substantial changes in the functioning of public services, with a shift towards the privatization of public management and a transfer to large private operators. In part, this was already present in Spanish society. For example, a part of the school system is controlled by private companies (mostly related to different parts of the Catholic Church), which receive direct subsidies from the state. The same situation occurs in the health care system. With the reforms, this model has become more deeply rooted, boosting privatization.

Figure 2 Employment trends in public sector and business sector, by sex, Spain, 2007–2013



Source: INE, Labour Force Survey.

Thirdly, and from our point of view a key aspect, there is the medium- and long-term impact of the measures being implemented in areas that directly affect the welfare of society, the operation of the labour market and a (possible) future growth model. The budget cuts and the changes in the public service provision model are likely to strongly affect Spanish society.

3.2 'Structural reforms' in education and training

The reforms undertaken by the government directly affect all the phases of working life, as described by Anxo, Bosch and Rubery (2010). Due to their recent introduction, however, the effects cannot yet be fully evaluated. A first area of transformation is found in the education system. Spain has long been characterised by educational deficits, reflected in a lower rate of people with higher qualifications and a high level of school dropouts. The main gap is in vocational training. Paradoxically, the percentage of people with higher education is higher than or as high as many of neighbouring countries. The school dropout rate has a clear social component and affects working class young people in particular. In recent years this process has been aggravated by the influx of people from other countries who were basically 'ghettoised' in state schools, while the private sector (with public funding) in effect engaged in 'social screening' (by various means, from the imposition of additional fees to direct discrimination).

The budgetary cuts applied by all the autonomous regions have a primary effect of further weakening the resources of the public school system, introduced mainly in working class areas. The implementation of the cuts is far-reaching and ranges from closing special educational provisions (such as groups with students with learning problems), eliminating support staff and reducing materials to the elimination of grants for extracurricular activities or replacing some qualified teaching staff with student teachers. Other major cuts have occurred in the policies affecting pre-school nurseries (for children 0–3 years). The universities have also suffered the serious effects of public funding cuts in three radical measures: an increase in entrance fees by around 100 per cent, a reduction in students' scholarships (raising the exam result threshold for access to the scholarships) and an increase in teaching hours (and the related laying off of temporary staff). The argument put forward to justify such measures is that there are too many university students, leading to

poor performance; higher fees are supposed to promote better educational achievement.

In this general context of cuts, the Popular Party approved a new education reform in 2013. One of the reform's main objectives is to restore the teaching of the Catholic religion as a central element of the school curriculum, in response to strong pressure from the ecclesiastical hierarchy (while at the same time eliminating 'citizenship education'). The most radical change is the introduction of new evaluation and selection mechanisms. These are aimed at classifying the school-age population and diverting schoolchildren whose academic performance is poor to low-level vocational training cycles from an early age. The model reflects the traditional perception of Spanish elites that society should be hierarchical and that it is not worth devoting much effort to improving the overall level of education. This seems to tie in with the economic vision that slashes spending on research, even though the unsustainability of the old productive model, with its focus on construction, is evident.

A second area of transformation concerns entry to the labour market. The high level of youth unemployment justifies the adoption of specific measures. The large number of temporary jobs and the long process of integration into the work environment, culminating at around 30 years of age, characterised the last period of economic expansion. This situation can be explained in part by the generalisation of temporary jobs to most of those entering the labour market, in all sectors. Furthermore, there are also labour market segments in which companies only hire young people under insecure conditions, such as retail, entertainment, fast-food outlets. In recent years this trend has been reinforced as the public sector has also increasingly opted for temporary employment.

The assumption on which the new measures proposed by the government rest is that youth unemployment is explained by young people's lack of adequate training and work experience (ignoring the fact that some young people had jobs before the crisis). Thus the plan of action is based on lower wages and reduced labour rights for young people, the idea being that they will be motivated to seek training. The most innovative element of the plan is that it effectively extends young people's job insecurity until 30 years of age. This is done by allowing companies to link work-experience contracts (with wages two-thirds of the minimum wage) which are designed for young people without training, with training contracts, designed for young people that are recently qualified. It is

sufficient for the young person to change jobs within the same company for another ‘new’ contract to be issued.

In the same way, this measure is applicable to anyone under 30 years of age, whenever they end their formal education. The plan also includes the introduction of a dual training contract (25 per cent working time in the first year, 15 per cent later); training can be done in the company, in a temp agency or in the form of online virtual training. The plan is supplemented by generous subsidies in the form of cuts in firms’ social contributions. Although some autonomous regions are considering the German-style vocational training development proposals, the general context of the cuts does not encourage the thought that there will be a real leap forward in the field of vocational training.²

3.3 ‘Structural reforms’ on the labour market

Undoubtedly the biggest change occurred with the labour reform passed in March 2012. In many ways the reform deepens what was already introduced in previous reforms in terms of making individual and collective dismissals easier (García *et al.* 2010; Fernández and Martínez 2013).³ The main novelty is the creation of a new type of contract that makes possible free dismissal during the first year, the liberalization of collective redundancies and the application of the same to the public sector (except for civil servants). The reform also confers important rights on companies with regard to internal flexibility and collective bargaining. The new framework grants individual companies enormous control over the implementation of collective agreements and changes in working conditions. In Table 3 we summarize the main changes introduced by the last two reforms.

-
2. The significant budget cuts in active employment policies which have been centred on occupational training policies and the promotion of local development also give rise to skepticism.
 3. The discussion of rigidity in the Spanish labour market is complex. Usually, it centres on the existence of highly protected permanent workers, but the real question is the provision in Spanish law that allows firms to dismiss workers with no need to justify their decision and without any announcement period, although at high cost. If firms do justify the dismissals the cost is much lower (and with the reform the dismissal cost with regard to a permanent contract can be the same as in the case of a temporary contract), but employers tend to use the expensive option because it is more flexible. Other things that provide a high degree of labour market flexibility include the diversity of collective agreements (at sectoral and territorial level), the extended use of outsourcing, the large proportion of small firms (which are not subject to certain collective agreement provisions), the lack of professional recognition that gives firms significant flexibility in using labour, tolerating informality and so on.

Table 3 Main aspects of latest two labour reforms, Spain, 2010, 2012

Aspect	2010 Reform	2012 Reform
Individual fair dismissal	Increased grounds, maintains compensation 20 days per year worked (of which 8 days are subsidised by the state)	Increases the grounds for dismissal Includes a drop in sales and future losses
Individual unfair dismissal (without good cause)	Reduces compensation for new contracts from 45 days per year (maximum 48 months) to 33 days per year (maximum 24 months) Void dismissal due to formal errors	Generalises 33 days per year compensation (maximum 24 months) to all contracts Eliminates interim wages
Collective dismissal	Introduces the option of temporary adjustment of hours	Eliminates public control of the procedure; companies can implement it unilaterally; extended to public sector
Temporary contracts	Introduces 12 days compensation per year worked Reduces the possibility of chaining contracts	New contract for SMEs with 1 year trial and free dismissal; chaining fixed-term contracts possible; generalises training and trial contracts (425 euros/month) for young people up to 30 years of age
Temporary employment agencies	Expansion of new sectors (construction) Ability to act as employment brokers	Possibility for temporary work agencies to work as private but public funded labour market intermediaries*
Internal flexibility	Increases the grounds for internal flexibility Company not required to comply with collective agreement	Unilateral right of company to change working conditions (mobility, timetable, etc.) if the employee does not accept it, fair dismissal
Collective bargaining	No change	Companies unilateral right to withdraw from collective agreement New time limit (one year) for collective agreement after expiry

* Delay in applying this reform mainly due to lack of funds to finance these private agencies, but the model is already established (and is manifest in the dismantling of public services in various autonomous regions).

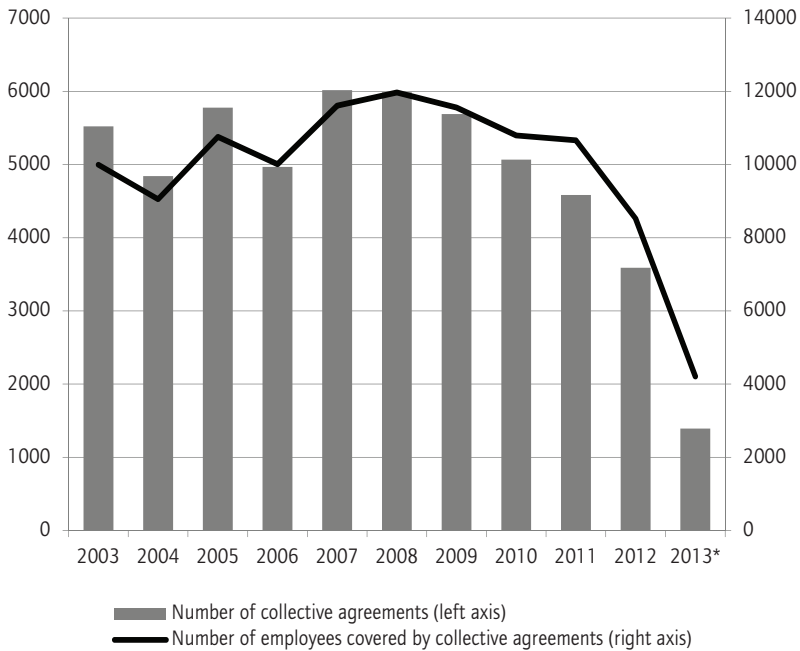
The most far-reaching change that has been brought about and may result in a radical transformation in working conditions concerns collective bargaining.⁴ Labour relations in Spain are complex. One aspect that should be highlighted is the low level of union membership and a production structure dominated by small businesses and temporary employment. Another is the regulation that grants a right to collective bargaining, at least to some extent. This applies in particular to sectoral agreements which, to date, were mandatory in all companies in a sector, whether they had union presence or not. This explains the high level of collective bargaining coverage despite the low level of trade union membership.

Pre-crisis labour legislation had conferred substantial social representation on the large unions and the *Ultra-Actividad* standard (which meant that the previous agreement is used as a floor for a new agreement and the agreement remains in force until a new one is negotiated) encouraged the maintenance of collective bargaining (Pérez Infante 2011). Although the fragmentation of negotiating spaces (both company agreements and sectoral agreements co-exist and may be national, regional, provincial or local) led to varying employment conditions between employees of different companies, sectoral agreements generated at least a basis of common social rights and established working conditions above the legal levels required by the Workers' Statute (which only sets the statutory minimum wage and statutory working hours).

This is the framework that the current labour 'reform' is destroying with a series of measures that, in practice, encourage the fragmentation of labour relations: company agreements take precedence over sectoral agreements; companies can unilaterally opt out of agreements; in companies with no union representative it is possible to negotiate with three employees chosen ad hoc (an excellent opportunity for companies to choose their counterparts in negotiations); and the economic effects of collective agreements cease one year after expiry.

4. An indication of the substantial nature of the reform is seen in how the reform was carried out. A month before its approval, the unions and the employers had signed a labour relations framework agreement, by which the unions hoped to limit the negative impact of the reform and trusted that the government would accept the agreement with the social partners. The government adopted the reform unilaterally, applying an emergency administrative mechanism (Legislative Decree) and ignoring any bargaining proposals (except those from other conservative parties that resulted in even more radical changes in some instances).

Figure 3 Collective bargaining coverage in the private sector, Spain, 2003–2013



Note: * Data for 2013 refer to October.

Source: Ministerio de Empleo y Seguridad Social, authors' figure.

Figure 3⁵ shows the dramatic fall in collective bargaining coverage over the past few years. Before the crisis, the percentage of private sector employees covered by collective agreements was 85–90 per cent. Within

5. This figure has some methodological aspects that we should take into account. Data refer to the total collective agreements that have economic effects during the year. Some of them agree in this year and other where agree previously but still are in force in the current year. In Spain collective agreements are “private” agreements between actors, and it is not compulsory to communicate immediately to the labour authorities. Sometimes social actors delayed long time (could be more than a year) the information to the Labour Office. Due to it, figures are continuously updated and, as far as the year, more accurate is the information. In this sense, figures referred to 2013 are dramatic but we need to take this prevention. Also, the information about the number of employees covered by a collective agreement is from the social partners, and is not comparable with LFS figures. Social partners not always know accurately the number of people involved in a sector.

only one year, 2011–2012, it dropped from 89 per cent to 76 per cent. It is important to note the soaring unemployment rate during the same period of time: the 89 per cent coverage in 2011 referred to 11.9 million workers in the private sector, while the 76 per cent coverage referred to 11.2 million workers; in other words, the number of people working in Spanish private sector companies covered by collective agreements fell by 20 per cent in the space of only one year. Though the data for 2013 presented in Figure 3 are provisional it is fair to assume that this downward trend has continued at a similar pace. It must be kept in mind that, when a collective agreement expires, the Workers' Statute is applied. The low level of the minimum wage (643 euros per month) leaves plenty of room for companies to implement wage cuts.⁶

The change in the collective bargaining model has three potential effects, which in some cases are already beginning to take shape. First, it promotes a wage devaluation (which contributes to weakening domestic demand).⁷ It also favours greater differentiation between working conditions at different companies. Finally, it signifies a direct attack on the unions, which can be removed from any regulatory capacity in sectors and companies with low membership.

The reforms have also directly affected the public sector. This sector has always been known for offering work-friendly conditions as regards stability, work balance and so on. Although public sector employees have already been the subject of unilateral pay cuts in recession situations (1993, 2010 and so on), the 'reforms' have now lowered public sector working conditions to the level of those in the private sector, with the exception of civil servants. This is accompanied by plans for outsourcing and closures, among other things. For example, significant budget cuts in research have resulted in collective dismissals, layoffs and status reductions (giving way to part-time jobs, for example) for many workers. This particularly affects the working conditions of people with higher

6. There are more and more cases of collective agreements in which companies impose pay cuts and worse working conditions. For instance in the collective agreement of large retailers wages have been frozen until 2016, a compensatory wage for working on Sunday has been eliminated, working time has been increased by 26 hours and working on Sunday is compulsory. Significant wage cuts have been reported from various important manufacturing and service companies.

7. From 2011 to 2013 the nominal wage increase agreed in collective agreements fell from 1.98 per cent in 2011 to 0.56 per cent in 2013 (Ministerio de Empleo y Seguridad Social, Boletín Estadísticas Laborales). Real wages per employee fell, on average, by 1.4 per cent a year from 2010 to 2013 (European Commission 2013).

education, who now see the traditional career model under threat. Since the public sector has always been more 'female-friendly' than the private sector, this change is particularly relevant in gender terms.

3.4 'Structural reforms' in the pension system

Major changes have also been made in the process by which an individual withdraws from the labour market, for example, as regards retirement conditions and pensions. Although Spanish spending on pensions is already well below the European average (9.2 per cent of GDP compared with 11.2 per cent), demographic forecasts and the higher pensions that those retiring in the next few years will receive were taken as an excuse to review the system. In 2011 the Socialist government approved a reform with the following main features: gradual extension of the retirement age from 65 to 67; lengthening of the contribution period which results in receiving the maximum pension (from 35 to 37 years); lengthening of the period of computation to calculate the pension (from 15 to 25 years); tougher voluntary early retirement conditions (only for workers at least 61 years of age in cases of collective redundancy and 63 in other cases) and replacement contracts (a formula by which older workers reduced their working hours to 25 per cent and in return the company hired a full-time worker). These last two measures seek to hinder the process of early withdrawal from the labour market, but also create new difficulties for employment adjustment processes and generational renewal.

In 2013, before the pension changes of 2011 had come into force, the conservative government launched a debate on the need for new 'reform'. The justification cited was the budget deficit of the social security system and, once again, demographic forecasts. In fact the current social security deficit is explained simply by the decline in employment and wages and their effect on social security contributions. This deficit is being met by a reserve fund created in the past to deal with adverse circumstances. A group of 12 experts (nine of whom are directly connected to the insurance sector) were tasked with producing a report whose proposals will form the basis for the new system. The basic idea is to adjust annually the amount of benefits according to the current level of social security contributions, which in practice represents a proposal to cut benefits.⁸

8. The formula proposed by the expert committee and introduced in the new legal draft means that annual pensions can increase (or decrease) according to the sum of the growth of

The new proposal offers no debate on the fairness of the pension system and the possibility of financing it from resources other than social security contributions. Neither does it explore demographic issues such as immigration or the role of the labour market (employment and wages). It simply introduces a new emergency debate. The changes have not been passed yet, but meanwhile the government has laid down that until 2019 pension increases will be only 0.25 per cent per year, justifying a further cut in social spending and opening the way to stagnation of private pensions.

Overall, mass unemployment has been used as justification for education, labour and pension changes which together will only heighten economic insecurity among the majority of people. They represent a substantial transfer of power and income to business owners and direct the exit of the crisis towards a permanent internal devaluation strategy. The growing inequalities between social classes and between groups of workers are spreading widely. We expect the next attack will come on unemployment benefits, which many mainstream economists consider too generous (although only 60 per cent of the unemployed are receiving unemployment benefit). The government has launched a propaganda campaign accusing many unemployed people of combining benefits with hidden jobs in order to justify the next round of cuts.

3.5 A package of conservative reforms

Amidst budgetary restrictions, reforms with a substantial social impact have been introduced in many key areas. The most important concern health care, justice, social services, housing, research and culture. In many of these areas, spending cuts have a direct effect on services and employment. For example, substantial research cutbacks are causing serious problems in the functioning of universities and research centres. This is a perverse departure given that technical change and innovation are one of the bases of competitiveness. Research cutbacks are in sharp contrast, for example, to continuing major financial support for the banking sector and car scrappage schemes.

8. (*cont. from p. 57*) contributions minus the growth of new entrants minus the growth of mean pensions plus 0.25 per cent of the surplus of pensions over expenditure. In fact it is a procyclical formula because in years of depression pensions will fall.

But the changes go beyond spending cuts to include systemic modifications. This is clearly the case with regard to health care. The government introduced changes to the health care model in April 2012. The most important is the discontinuation of universal health care, introduced in 1986. Illegal or irregular immigrants are now entitled only to emergency care. People over 26 years of age who have not yet paid social security contributions and other minor groups will no longer have access to some health care benefits or only under certain circumstances. Furthermore, the co-payment ratio in medicines has been increased and extended to pensioners – who were previously exempt – medical transport and prostheses.

Also, more than 400 medicines have been excluded from social benefits – including many used to treat everyday illnesses – while, to add insult to injury, the government is refusing to implement the genuine reform that most health experts suggest to reduce spending, namely central purchasing of generic medicines by auction and direct supply. In parallel, many regional governments, which manage the bulk of health care, are introducing an intensive and partial or total privatization programme in the health care system. This is a shadowy process in which a number of coincidences between the interests of public managers and private holdings have been observed and more than one case of corruption has been exposed. On the whole, the measures will put increased pressure on lower incomes and reinforce a segmented health care model characterised by social discrimination.

The administration of justice is also under attack from ‘reformers’. Leaving aside the various changes introduced in the organization of the *Consejo General del Poder Judicial* (General Council of the Judiciary), aimed at facilitating control of the entire judicial system by the government, one major element that affects people’s daily lives is the introduction of an expensive system of court fees generating costs that are unaffordable for most people. This has had a huge impact on people’s ability to obtain recourse to the courts to combat abuses suffered in all areas, including employment, the financial system, housing rights and so on. Lawyers have already observed a significant reduction in resort to the law, in the context of what they consider the development of a justice system exclusively favouring the rich.

Something similar has happened with housing, one of the most serious problems associated with poverty. Housing was one of the main ele-

ments of the speculative asset bubble and its bursting has left thousands of people with serious debt problems and facing eviction. While in other areas the government has fallen over itself to introduce ‘reforms’, in this instance it has acted only in response to the powerful social movement of those that have been evicted. But only tentative steps have been taken, in part imposed by the European Union, and the overall situation has not been addressed. Indeed, new regulations have been passed on rental properties that make it much easier to evict tenants (eviction is now automatic if the tenant is one month behind with the rent, as is the tenant’s entry in a public register of debtors) and to implement frequent rent reviews.

Last but not least are the changes to social services concerning dependency benefits (for elderly and severely disabled people). The law passed in 2008 tried to address the problem of aging and to improve the balance between family care and personal life, especially for women, who continue to shoulder the principal care-giving burden. Although the reform was inadequate – the highest benefits were given to women caring for relatives at home – it paved the way for a new approach and to some extent favoured the development of employment in the sector. The new policy, however, follows the same line as the one proposed in health care: to cut benefits, introduce co-payment for services and eliminate the social security coverage to which family caregivers were hitherto entitled. Once again, care-giving is officially regarded as a ‘family matter’, above all for females (Torns and Recio 2012).

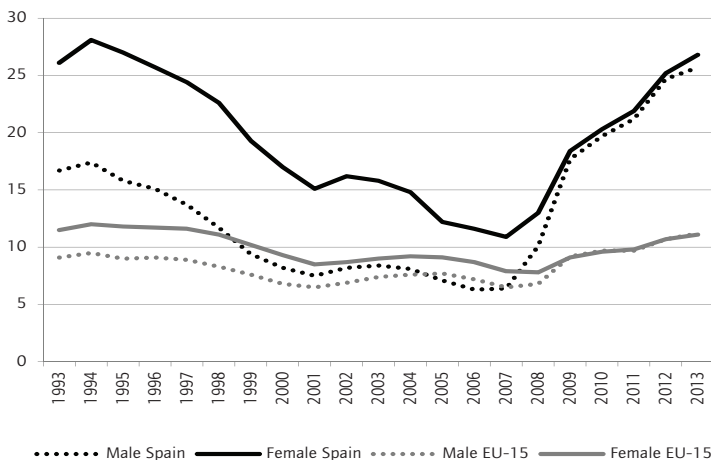
The policy of cuts is not merely a temporary adjustment in anticipation of better times. Rather the government has taken the opportunity offered by the crisis – ‘never let a good crisis go to waste’ – to pursue as many ‘conservative’ policy aims as it can, for example, opening up new business opportunities – in health care, education and insurance – to private financial interests. The changes it is implementing form part of an overall project to diminish social rights, further empower financial capital and implement conservative ideology. This is at the expense of, among other things, scientific and technological development, the promotion of a more cooperative and productive economic system and the elimination of social barriers, not to mention the fact, for example, that many privatisations end up mired in political corruption, still one of Spain’s endemic problems.

4. Labour consequences of the crisis

The most prominent impact of the crisis is rising unemployment (Figure 4) and massive job destruction, which was particularly dramatic in 2008–2009 (mainly related to the bursting of the construction bubble) and 2012 (directly related to public sector ‘adjustment’ and labour market changes) (Lago Peñas 2013; Recio 2013). In 2013 the unemployment rate was over 26 per cent, in some regions more than 30 per cent and for young people between 16 and 19 years of age a horrendous 65 per cent or more. The situation becomes even more disturbing if we take into account the growing number of people simply giving up active job search, swelling the ranks of the discouraged.

Besides the high unemployment rate, since 2012 more than 50 per cent of unemployed people have been in this situation for longer than a year. In addition to the stigma attaching to unemployment and the personal demoralisation that goes with it the unemployed also suffer from low incomes; in Spain unemployment benefits are time limited and social protection is low. The system is based on a contributory benefit which establishes the right to receive an income equivalent to 70 per cent of the

Figure 4 Unemployment rate by sex, Spain, EU15



Source: Eurostat

Figure 5 **Percentage of unemployed people receiving unemployment benefit, Spain**



Source: INE, INEM.

basic wage for the first six months and 50 per cent thereafter (previously 60 per cent, but reduced in 2012) in the proportion of one month's benefit for every four months' contributions (with a minimum contribution period of 12 months and a maximum of 24 months' benefit). On expiry, people can access a contributory benefit for a maximum of 24 months, equivalent to 66.6 per cent of the statutory minimum wage. This is not a universal benefit but is granted to people based on their particular circumstances (age, family status).

As a consequence, the share of unemployed people without benefit has grown rapidly (Figure 5).⁹ In response the government established a new

9. The quantification of people receiving unemployment benefits is subjected to dispute (Figure 5). One formula for this calculation is the ratio between unemployed individuals receiving any type of benefit and the number of people registered as job seekers in employment offices (to which we should add temporary agricultural workers receiving a special unemployment

benefit of 400 euros for unemployed people without income in 2010. This is not universal either and depends on the current level of unemployment. In this context an increasing number of unemployed are left without benefits, thereby opening the way for growth of informal employment.

The crisis has also changed the gender pattern of unemployment and the labour force. Analysing the origin of unemployment, for men the economic crisis has reduced the active population and employment opportunities, which means that the upsurge in unemployment is basically explained by the disappearance of jobs. For women, the labour force has increased significantly and jobs are not being destroyed with the same intensity.¹⁰ The unemployment rate of reference persons (heads of household) has grown at a much faster rate compared with previous crises, in which the highest unemployment rate increases were recorded among partners and daughters of the reference person (Toharia 2003).

This has major implications for incomes and for labour mobilisation. In previous crises the job of the head of household cushioned the shortfalls in the unemployment protection system, when other members of the family were unemployed. At the same time, lower levels of debt and higher levels of household income, compared with the present situation, made it possible to 'navigate' the labour market under better conditions. In the current crisis, however, the very high level of household debt is accompanied by major job destruction among heads of household, thus forcing a more intense integration into the labour market by other members of the family unit, all in a context in which job opportunities are practically non-existent.

During the first phase of the crisis, there was a substantial influx of new female workers to the labour market. These newcomers were mainly women over 30 years of age, which indicates a change in family roles in search of employment. This situation has reversed since 2012, when the persistence of massive unemployment started to generate a dominant 'discouraged worker effect', with the result that exits from the labour market

9. (*cont. from p. 62*) benefit). In this case, the coverage rate during the last quarter of 2012 was a little over 60 per cent. However, if we consider the number of unemployed people receiving any unemployment benefit in relation to the (higher) level estimated by Eurostat this indicator goes down to 50 per cent for the same period.

10. Among immigrants the trends differ somewhat. The decrease in the immigrant male active population is higher compared with the Spanish population. Among women, the immigrant active population is falling, while among the Spanish population it is rising substantially.

– which had already been taking place among young people – helped to reduce the unemployment rate. Emigration – mainly among recent immigrants – has also had an effect, in addition to less intense job search. All these trends are substantially modifying the characteristics of the labour force in Spain, as well as the dynamics of household labour market strategies. The substantial increase in workers in a vulnerable position in the labour market makes it much easier to implement more backward-looking labour management practices and is creating a growing group of marginalised workers. At the same time, the traditional emphasis on the family as ‘provider of welfare services’ has resumed performance, in a context in which the public sector is no longer providing basic services. All in all, there is a notable risk that this dynamic will become deeply entrenched in the social structure, especially if the more regressive measures are sustained or even intensified, thus consolidating a marginal workforce and marked and widespread social regression.

The high unemployment rates and limited coverage of unemployment benefits have a direct consequence on incomes and well-being. But workers are also being affected by the crisis. Besides the increase in insecurity and deteriorating working conditions, wages have decreased dramatically (ILO 2013) (see Figure 3 in the chapter authored by Schulten and Müller). According to Eurostat, the ‘in work at risk of poverty rate’ data show that in 2007, 10.7 per cent of the employed had an income lower than the poverty level, and in 2011 this percentage was 12.3 per cent. The causes of this trend are to be found in the wage moderation negotiations that took place at company level, the collective wage bargaining reform that has allowed a substantial fall in negotiated wages and wage cuts in the public sector.

The final effect of all those trends is falling income. Job destruction, low social benefits and diminished coverage, wage moderation in both the public and private sectors, the freezing of the statutory minimum wage, pensions and withdrawal of social assistance, as well as price increases have entailed a significant loss of household income, with a sharp fall in disposable income (Consejo Económico y Social 2013). According to survey data, disposable income has declined more than 10 per cent since 2007 and income inequality has greatly increased. The Gini index has increased by almost 10 per cent and the difference in income between the 80th and 20th percentiles has risen by almost 30 per cent since the beginning of the crisis (Fundación Foessa 2013).

5. Conclusions

After nearly seven years of economic crisis, Spanish society remains in a dire situation. In our previous papers in the Dynamo project we highlighted the weaknesses and contradictions of the Spanish employment model. Specifically, we noted that the model's dynamics were marked by a certain opposition between a neoliberal economic policy orientation and a strong social demand for social democratic measures of the kind that had led to the expansion of public services. The Socialist Party, ruling from 1982 to 1986 and from 2004 to 2011, reflected this contradiction, with its neoliberal economic orientation and progressive social policies (although limited by insufficient resources). Although the 1986–2004 conservative governments introduced substantial regressive elements, circumstances forced them to retain part of the acquired social rights. Maintaining a balance between these two contradictory dynamics was possible for a time because of a favourable international situation and the influx of resources from outside. The latter helped to unleash the huge speculative bubble that supported much of the expansion cycle. At the same time, it undermined alternative development possibilities. When the crisis and the end of the model became apparent, the result was disastrous for social democratic policies.

The combination of a doggedly conservative government, in both economic and social matters, the pressures emanating from the European Union and the accumulation of problems (especially those of external debt and fiscal crisis) has given rise to a neoliberal-conservative programme. This is reflected not only in the policy of budgetary cuts but also in major 'reforms' that tend to further weaken the social position of workers and unions, and to promote the policy of handing over public policy to economic interests. In part this represents a resumption of the old Mediterranean model, as many of the cuts are aimed at shifting social burdens onto families, especially women, to fill the gaps opened up by the lack of public provision. The fact that the reform programme does not provide impetus for technological change and product innovation reflects the conservative elite's attachment to instigating a new speculative cycle, as manifest in the various measures taken in urban planning, including a new coastal law, the granting of residence permits to home-buyers, city-casino projects and so on).

This inward economic colonisation is devastating for many Spanish people, who are experiencing developments with a certain helplessness,

exacerbated by the apparent impunity with which corruption is proliferating. The most tangible short-term results include the maintenance of a very high unemployment rate and rising inequalities and poverty; expansion of the informal economy; deterioration of public services; and sustained recession; which is closer to the experience of many Latin American societies affected by adjustment plans rather than the Central European model that Spain has spent years trying to emulate. The 'new' model that the current government is promoting is reinforcing an obsolete production model based on low wages and precarious employment, limiting the possibility of change and reproducing all the problems that have traditionally afflicted the Spanish economy. It represents a resumption of a growth path based on low prices and wages, a model superseded by central and eastern Europe in the 1990s.

Spain is suffering under a bankrupt economic model without expectations of change, but rather of further shock-waves, on top of those that have already occurred, such as the mass evictions and VIP scandals that provide glimpses of an ongoing social despoliation. Furthermore, the advance of neoliberal policies is occurring in the absence of clear alternative proposals. Although there are important social movements against government policies (such as 15-M, Foro Social and PAH, the group concerned with mortgage problems) they focus on specific issues. There is no clear alternative to austerity and neoliberal policies. Neither the opposition parties nor the trade unions have offered substantial plans for new development paths. In the absence of a credible political alternative to the neoliberal policy of cuts and labour market deregulation the latter can be propagandised as the 'only realistic answer' to the crisis.

The desperately needed turnaround will be very difficult, if the orientation of EU policy does not change. And this is without even considering what might happen if economists' worst predictions regarding the ecological crisis come true. Spanish society requires long-term strategic proposals that, in our opinion, should include the following:

- A realistic plan for transforming the production structure and for reforming the skill formation system needed for this change, in order to improve the external balance. This transformation also needs to confront the challenge of environmental sustainability.
- Reform of the tax system in order to fund an adequate welfare system and recovery policies. Reform must also introduce progressive treatment of incomes.

- Reform of labour institutions and company organisation in order to promote decent jobs in terms of pay, skills, cooperation, working time and so on. A new model must guarantee an adequate balance between working time and private life.
- Recovery of control over the financial sector in order to halt the financialisation of the economy.

There is no evidence that accumulating austerity and neoliberal measures will drive an economic recovery. The balance of power between labour and capital has changed dramatically in favour of the latter. Political reforms have eroded the effective civil rights of the majority of people. Troika pressures continue to demand more ‘reforms’ in the same direction. Spanish economy and society are trapped, at least in the medium term, plagued by stagnation, massive unemployment and stark inequality in a country that has returned to ‘exporting’ workers. Spain is to some extent experiencing a return to the past, experiencing the adjustment policies that affected Latin American countries some years ago. We need different ideas and different policies, at both national and European level. If they are not forthcoming it is likely that Spain will face a long period of social stagnation, suffering and uncertainty: a deep crisis within the crisis.

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Italy's long stagnation

Annamaria Simonazzi

Bare virtue can't make Nations live
In Splendour. They that would revive
A Golden Age, must be as free,
for Acorns, as for Honesty.
Mandeville, *The Fable of the Bees* (1705)

1. To have and have not

Italy is trudging through a horrendous sixth year of recession. The dismal results of the first half of 2014 only confirm the severity of the depression, the worsening of the 'fundamentals' and the ineptness of the policies implemented in these years. As a result of a continuous, severe downturn, only briefly interrupted by an almost imperceptible recovery, Italy's GDP reverted to the level of 2000, 9 per cent below the level of 2008. Despite continuing fiscal austerity, the loss in output had swollen the debt/GDP ratio to 135 per cent by August 2014. Italy's predicament is shared by the other countries on the European periphery, which are struggling with negative growth rates (see Figure 1 in the introductory chapter of the present book), record high unemployment and increasing (private and public) debts. As of March 2014 sovereign debt to GDP was 124 per cent in Ireland, 132.9 per cent in Portugal, 96.8 per cent in Spain and 174.1 per cent in Greece.

Things are different in Germany. Its GDP has reverted to – and surpassed – the pre-crisis level. Its labour market is humming: employment has risen by 3 million in the past decade and unemployment has fallen to 5.2 per cent, a post-reunification low and the second-lowest level in the EU28. Its current-account surplus has averaged nearly 7 per cent of GDP since 2006, reaching a new peak of 7.5 per cent in 2013: the surplus with other euro members fell from 4.5 per cent of GDP in 2007 to 2.1 per cent in 2013 because of their negative growth, but high-investing emerging markets have filled the void. Public finances have been flourishing, buoyed by healthy tax revenues, ultra-low long-term interest rates – in part due to Germany's status as a haven during the euro crisis – and fiscal restraint. In 2013, for the first time since 1950, the public debt fell

by 1.5 per cent and the federal government expects its debt as a percentage of GDP to fall from nearly 80 per cent to under 70 per cent in the next three years. These economic and fiscal successes continue to make Germany a bastion of strength in the fragile euro zone. No wonder that, according to a recent Eurobarometer poll, 84 per cent of Germans are satisfied with the state of their economy (Economist 2014).

Such radically diverging fortunes within the euro zone are astounding and hardly sustainable. How did we get here and where are we going? This chapter offers an interpretation of Italy's vicissitudes, starting with a brief overview of the Italian economy before the outbreak of the crisis (Section 2). It then surveys the policies implemented in the crisis and their effects on the productive and social fabric (Sections 3 and 4). The chapter concludes with an assessment of the – national and European – alternative policies for recovery.

2. Two decades of slow growth

Reforms: not far enough?

The currency crisis of September 1992 and the ensuing severe recession marked a watershed between two different economic policy scenarios. With the decision to enter the Economic and Monetary Union (EMU), the European Monetary System (EMS) first and the EMU afterwards provided the legitimacy – on the grounds of external constraint – for unpopular policy measures aimed at coping with structural disequilibria. Major supply-side reforms were implemented in the aftermath of the 1992 crisis in the areas of the labour market and industrial relations, privatisation and corporate governance, administrative decentralisation, pensions and social protection.¹ They shared the common principle of 'letting the market work'. However, while the *pars destruens* was fully or partly implemented, the *pars construens* was constantly delayed: due partly to budget and external constraints, proposals fell by the wayside during the many phases of legislative proposals, parliamentary debates, legislation and implementation, until a new government changed the agenda. Thus, labour market reforms to implement 'flexibility' were not accompanied by reform of the so-called 'shock absorber' systems (for

1. See Simonazzi (2014) for a brief analysis of the various reforms.

instance, truly universal unemployment benefit schemes or income support policies); reforms of the goods market have been limited to privatisation and unaccompanied by true liberalisation; social expenditure has remained limited to monetary transfers, with ever lower social investment; and social care has been left entirely to the family (and to religious or voluntary organisations) and, increasingly, to the (irregular) market. The result has been a set of partial, incomplete and incoherent reforms that have not changed the main features of the Italian welfare state, but have rather accentuated its segmentation and lack of universality.

Despite these far-reaching reforms, since the late 1990s growth has fallen below the EU average. This lack of growth has puzzled the (mainstream) economic community, which has sought a scapegoat by claiming that the reforms were not far-reaching enough.² A 'divided society ... less based on (declining) ideologies and more on the gradual proliferation of many consolidated interest groups, each one seeking to gain rents at the expense of others' (Crafts and Magnani 2011: 20) and the veto power of the opposing actors were offered to explain why reforms fell short of what was required to tackle the challenge of a radically changed economic environment (allegedly because of technical change and globalisation).³

Decline?

The extremely low rate of growth gave support to the hypothesis of a long-term economic decline. The decline story maintains that firms' size and industrial specialisation resulted in a lack of product and process innovation leading, in turn, to a loss of competitiveness, as evidenced by, among other things, the decline in Italy's export share. Labour reforms and the deregulation of the labour and product markets were deemed necessary to resume growth.

This interpretation, which enjoyed increasing popularity to become the consensus view, had come up for reconsideration in the very years

2. For instance, Crafts and Magnani (2011: 20) argue that 'supply-side reform did not go far enough especially given the context of joining the Eurozone. In several respects, including the legal system, competition policy, regulation and privatization, reforms were either incomplete or inadequately implemented.

3. 'The general story is not that regulation has become more stringent but rather that existing regulation became more costly in the context of a new technological era' (Crafts and Magnani 2011).

preceding the crisis. Firm-level evidence from Italian manufacturing confirmed that low-tech businesses, which arguably benefited most from currency devaluation, had been restructuring more since the adoption of the euro. Restructuring entailed a shift of business focus from production to upstream and downstream activities, such as product design, advertising, marketing and distribution, and a corresponding reduction in the blue-collar workforce. The process of change had been led by medium-sized firms, firmly rooted in district economies (Coltorti 2007), and had been accompanied by outsourcing (Breda and Cappariello 2010). The new challenges posed by globalisation, the diffusion of information and communication technologies (ICT) and the adoption of the euro induced the most dynamic Italian firms to rethink their organisation and degree of vertical specialisation. The conclusion was that, since the adoption of the euro, a reallocation of activity had occurred within rather than across sectors, supporting the productivity growth in those sectors that had once relied more on competitive devaluations to regain price competitiveness (Bugamelli *et al.* 2009). While this evidence cut the link between the data on 'frozen specialisation' and the hypothesis of a lack of innovation and restructuring, it also made evident that the crisis had hit Italian medium-sized firms just as they were crossing the ford.

There are three main weaknesses in this rejuvenation process:

- (i) Restructuring has not been supported by an adequate expansion of the domestic market. The labour market reforms of the late 1980s and 1990s resulted in an increasing share of precarious, badly paid jobs and stagnating real wages. Two major consequences followed: on one hand, the stagnation in consumption accounted for the limited expansion of the productive capacity; innovative firms focussed more on the efficient exploitation of existing capacity than on the expansion of new capacity, making a productive base too small to absorb the entire labour force at fair wages; on the other hand, the creation of an ample reservoir of cheap labour allowed the survival of marginal firms.
- (ii) Widening of the north/south divide: from the mid-1990s the gap in per capita income had started to increase again. In 1992 the Cassa per il Mezzogiorno was dissolved, ending active industrialisation policy. However, southern Italian industry was too fragile to stand up to the harsh competition of a monetary union unaided: it is more dependent on domestic demand; the incompleteness of its value chains makes it dependent on external inputs, so

that the leak of imports from the centre-north weakens the correlation between the expansion of industrial production and the growth of the chain;⁴ finally a much higher share of firms in the southern value chains are in a weaker contractual position than their northern counterparts. Since the inception of the common currency the gap between the south and the centre-north of Italy has widened again (and has got worse in the crisis).⁵

- (iii) Micro-led restructuring, without a macro framework. The process of restructuring has occurred in a void of national coordination and guidance and the crisis has accelerated the trend, inducing even more fragmentation.

There was – and remains – little awareness on the part of the economic mainstream of the inadequacy of supply-side reforms to encourage the adaptation of a relatively still backward economy to the new context. Aggregate demand had no explicatory role in the interpretation of the slow growth of the Italian economy: the effects of these reforms, and of the macroeconomic policies implemented in the period, on income distribution and domestic demand were simply neglected. Thus, the long, painful period of cutbacks that started in the 1990s had no corresponding results in terms of improved public finances.

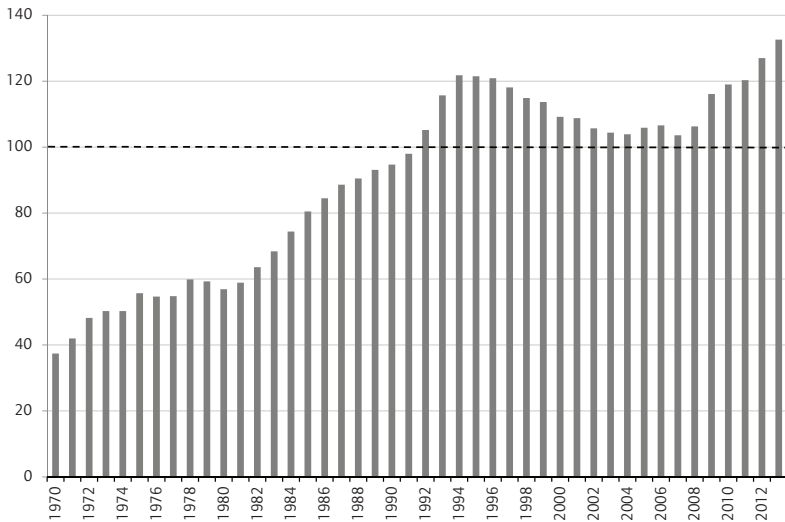
Public debt

The build-up of public debt occurred in different steps, sustained by various causes (Figure 1). The implementation of several social reforms in the 1970s (employment and pension schemes, health care and education) had resulted in a rise in public spending without a corresponding increase in tax revenues. The financing of the 'southern welfare model', which was still far from ensuring universal coverage, was thus provided by borrowing. The need to support the restructuring of Italian industry in the difficult decade of the 1970s provided a further exacerbation of public deficits.

4. Bronzini *et al.* (2013) have estimated the degree of completeness of the value chains, showing that the linkages (measured in terms of additional workers) activated in the south are seldom greater than half the number observed in the centre-north.

5. As observed by Faini (2003), if southern Italy had grown at the rate (2.9 per cent) achieved by the 'Cohesion countries' in the 1990s Italy's rate of growth would have been half a percentage point higher and there would never have been a debate on economic decline.

Figure 1 Debt as a percentage of GDP, Italy, 1970–2013



Source: European Commission, General Government Data.

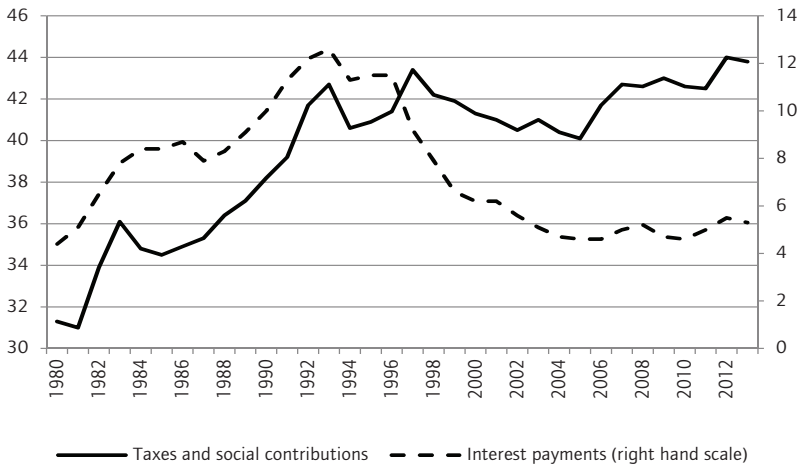
The policy of fixed exchange rates (EMS) in the 1980s, in a period of worldwide disinflation and high real interest rates, brought real interest rates to levels never seen previously. In combination with the prohibition on monetising the debt, introduced in 1981, this further fuelled the debt. By 1992 the tax/GDP ratio had increased⁶ (remaining above 40 per cent since 1991 and rising to 44 per cent in 2012), but the 10 percentage point increase of the 1980s went to service the debt: between 1990 and 1996 interest payments stayed constantly above 10 per cent of GDP (Figure 2).

Lower taxes for all!

In the two decades of predominantly centre-right government a series of tax reforms have been passed: fiscal amnesties (several waves since

6. At 34 per cent, the ratio of fiscal receipts to GDP at the beginning of the 1980s was 12 percentage points below the level of France and Germany, but reached the value of the German ratio by 1992.

Figure 2 Fiscal revenue and interest payments as a percentage of GDP, Italy, 1980–2013



Source: Bank of Italy.

1994) and no-prosecution for those returning illegally exported capital (fiscal shield 2009); elimination of inheritance tax (2001) (reintroduced by the centre-left government in 2006 for the very largest properties); and abolition of the local tax on first homes (2008) (which represented local authorities' most important source of revenue). The reduction in the tax burden from the peak reached in the late 1990s – to qualify for admission to the EMU – did not benefit everyone in the same proportion. Toso, Baldini and Morciano (2007) have assessed the distributive effects of the fiscal reforms of the Berlusconi II government (2001–2005): they estimate that 2 per cent of the total fiscal advantages accrued to the 10 per cent at the bottom of the income distribution, while 20 per cent have gone to the 10 per cent at the top. All in all, more than half of the total fiscal benefits have gone to the top 40 per cent.

Lower taxes demand spending cuts to keep the deficit from exploding. Social spending – education, research, social services and so on – have been at the forefront of any financial law aimed at coping with the umpteenth financial crisis; in fact, badly needed social reforms did not even take off: no support to families for child care and long-term care for de-

pendent people, no policies for young people, no minimum income for the needy and no equal rights to protection.⁷ Personal services have continued to rely almost solely on the family⁸ and the (irregular) market. Of the much trumpeted flexicurity, only the first part was implemented.

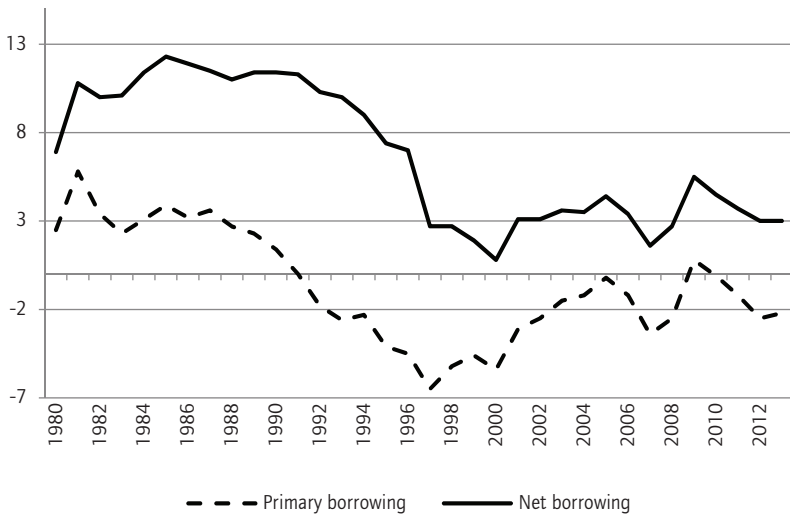
To conclude, since the 1980s the economic scene has been dominated by public debt. The debt/GDP ratio reached a peak of 120 per cent in the aftermath of the 1992 currency crisis; fiscal austerity in the second half of the 1990s and declining interest rates in the first years of the EMU lowered it to 103 per cent of GDP in 2007, just before the outbreak of the crisis. The service of the debt fell from its peak of the mid-1990s, but hovered around 5 per cent of GDP for most of the following decade (Figure 2). The debt and its servicing have represented the main, perverse channel of income redistribution, eating away the primary surpluses which have had to be squeezed out of the economy ever since 1992 (Figure 3). The middle classes (and the ‘third Italy’ in the north-east and elsewhere) managed to avoid paying taxes and turned their tax notices into bonds, underwriting the loans required to finance the deficit (Barba 2011). Through tax evasion, tax avoidance and tax cuts fiscal policy had three main effects: perverse redistribution, erosion of the basis for financing social policies and the unleashing of a political race that made tax reduction a bipartisan policy objective.

3. The crisis: reinforcing the features of the model?

At the outset of the crisis,⁹ the weakness of the public budget made it difficult to counteract its effects with an expansionary fiscal policy: according to IMF estimates, Italy’s fiscal stimulus over 2008–2010 amounted to 0.3 per cent of GDP, compared with an average of 3.4 per cent for the main advanced economies, and it was achieved mainly by changing the composition of the budget, leaving the balance unchanged. Nonetheless, the depth of the economic crisis took a heavy toll on the public finances:

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7. The introduction of a social card for families below the poverty level, extension of the no-tax area and increased allowances for lower income families (minimum pensions, one-off allowance for the first baby) were the main pillars of fiscal and social policy.
 8. This was made the government’s official policy in the White Book of the Minister of Labour, Health and Social Policy (Ministero del Lavoro 2009), which has put the family firmly at the centre of welfare.
 9. This section draws from Simonazzi (2014).

Figure 3 Primary and total net borrowing as percentage of GDP, Italy, 1980–2013



Source: Bank of Italy.

in two years the debt/GDP ratio increased by 13 percentage points (from 103 per cent in 2007 to 116 per cent in 2009). Thus, when in 2010 the worst seemed to be over, the efforts aimed at reducing the deficit were resumed, mainly through cuts in expenditure.

Once again, the fiscal austerity measures implemented in the crisis lacked coherence and good design. This can be explained by a combination of the usual factors:

- the alternation in government of political forces with different political and philosophical orientations, mid-way between neo-liberalism and populism on the part of the centre-right, biased in favour of so-called ‘market efficiency’ as a path to sustainability, and social inclusion on the part of the centre-left;
- the lack of vision of the centre-left parties, divided between the assumed necessity for fiscal consolidation and the means to achieve it, on one hand, and the political race to implement tax reductions, on the other;

- the weakness of the trade unions, victims of their own divisive policies and their inability to represent the interests of marginalised workers and, especially, young people; and
- perverse redistribution and reduced tolerance for inequality, which has taken the form of demands for the reduction of ‘privileges’ but not for the extension of rights (universalism).

The result has been:

- further reduction of social investment;
- privatisation of parts of social expenditure and individualisation of risks, with the ‘exit’ option encroaching on health, education and personal services;
- institutional fragmentation; and
- geographical polarisation.

The commitment to reducing the debt/GDP ratio, undertaken in the Fiscal Compact, and the inclusion in the Constitution of the obligation to balance the budget will continue to impose restraint on fiscal policy in a period of persistent deep economic recession.

Austerity packages

The sovereign debt crisis, which started in July 2011 with a sharp increase in the interest rates on Italian government bonds (the yields on Italy’s 10-year bonds increased by 200 basis points, from around 5 per cent in early July 2011 to around 7 per cent in November 2011) forced (or, according to some, was instrumental in) the pursuit of fiscal consolidation. Three austerity packages were approved over a short period of time. The first two were presented by the Berlusconi centre-right government in August and November 2011. The last and tightest one was approved in December 2011 by the coalition government led by Mario Monti.

The policies implemented responded primarily to the commitment to fiscal consolidation. Budgetary measures (tax increases and spending cuts), sale of public assets and structural reforms (labour, pensions, liberalisation of strategic sectors) have been variously announced, implemented and amended by the ensuing governments.

Spending cuts consisted mainly of draconian reductions in financial transfers to local authorities and public spending for health care and education. The freezes in labour turnover and wages introduced by the Berlusconi governments since 2008 were extended in 2013 and 2014: recruitment of new permanent staff was frozen until 2015 and limited to replacing only part of the turnover thereafter. Due to these measures, since 2006 public employment decreased by 8 per cent (280,000 people), of which 70 per cent was in education (Banca d'Italia 2013). The Health Fund was repeatedly cut, endangering adequate health care.

A new wave of reforms

At the peak of the financial crisis, the new Monti government hastily passed reforms aimed at arresting the financial meltdown by reducing expenditure (pension reform) and by sending a strong signal to other countries and creditors (the labour market reform).¹⁰ These measures, rashly prepared and hastily passed in a vote of confidence, have produced unintended short and long-term effects that the following governments are still striving to put right.

Pension reform

The Fornero-Monti reform (2011) increased the minimum retirement age to 66 years, eliminating all forms of flexibility. With pension benefits strictly linked to contributions, it introduced an unnecessary rigidity in the retirement age. Precipitously and rigidly applied to respond to the urgent need to cut spending and appease the financial markets (as well as EU and German authorities), this reform left several short- and long-term problems open. While the Italian pension system has become the most rigorous among the EU systems (Banca d'Italia 2014), it is also the least adequate in terms of pension income and the most ineffectual with respect to the broader objectives of productivity, growth and employment (Pizzuti 2013). Two main trade-offs, which derive from the interrelation between the pension system, the labour market and the welfare state, threaten its long-term sustainability. By extending the working life

10. Changes in the labour market in the direction of still greater flexibility were among the conditions set out in the letter sent by the ECB in August 2011 to the Italian government spelling out the basis for its support to the Italian bond market.

of older workers, this reform ends up by keeping young people out of the labour market (and forcing down their wages), with negative long-term effects on productivity and growth, given, as is usually maintained, that young workers are more attuned to new technologies. It has also made reconciliation more difficult, especially due to the simultaneous cuts in social expenditure. The combination of an intermittent working career (due to maternity and care duties) and a pension system strictly based on contributions is likely to make economic self-sufficiency in old age more and more difficult for older women to achieve. Nor is it likely that the second, private pillar can be relied upon to complement meagre future pensions. Finally, pension reform and action by the subsequent government have failed to achieve more equity among current pension recipients. Pension benefits are very unequally distributed: the 33.5 per cent of men and 53.5 per cent of women who receive a pension below 1,000 euros per month account for 12.3 per cent and 28.2 per cent, respectively, of total pension expenditure; while the 8.4 per cent of men and 2.3 per cent of women who receive a pension above 3,000 euros account for 23.6 per cent and 8.5 per cent, respectively, of total expenditure (Istat 2013). The unfairness at the basis of the institutions of social protection has not only failed to prevent the fall into poverty of a large number of families but it has even contributed to an increase in inequality.¹¹ While the backbone of the pension reform is unlikely to be reversed, the following governments' willingness to amend some of its shortcomings – such as the elimination of the fixed age of retirement in favour of a flexible range and the problem of pension rights below the poverty line because of precarious and discontinued careers – has been stalled since these adjustments are deemed too costly for the time being (Giovannini 2013).

Labour market

Labour market policies have pursued three goals: increase flexibility; lower labour costs; and favour the employment of vulnerable categories via tax credits and subsidies.

11. It has been estimated that '21.4 per cent of expenditure goes to close the gap between the pension computed on an actuarial basis and the minimum pension (so-called 'integrazioni al minimo', 495.43 euros a month in 2013) and 13.1 per cent of social pensions, amounting to 2.8 billion euros, go to families in the highest deciles (8, 9 and 10) of the income distribution, as determined according to the new ISEE (*Indicatore della Situazione Economica Equivalente*, an indicator of the household's economic condition), with an average equivalent disposable income at or above 210,000 euros per year' (Baldini *et al.* 2013).

Calls for further liberalisation of the labour market have come from many quarters, including the ECB, the European Commission and the financial industry. Inspired by various European 'best practices' – from Danish flexicurity to the German apprenticeship model – the labour reform passed in 2012 had ambitious goals: on one hand, it aimed at reducing precariousness by re-regulating atypical contracts and extending the coverage of social protection,¹² and on the other, it was intended to make redundancies easier. The reform pleased no one: it met with criticism from firms for making atypical labour more expensive; it raised strong opposition from the trade unions for its attack on labour protection; and it frustrated the aspirations of the weakest segments of labour – women, young people, precarious workers – for its failure to tackle existing inequalities in labour rights. The part of the law targeting precariousness was soon substantially overhauled by legislation.¹³

An important corollary of the flexibility approach – and one that meets with the general support of government, trade unions and firms – is the need to reduce labour costs to increase employment. The Monti government's effort to improve access to jobs for women, young people and vulnerable categories of workers relied basically on a series of employment subsidies: tax deductions for firms (for example, IRAP¹⁴) and reductions of employers' social contributions with regard to newly hired 'weak' categories of workers or conversion of temporary contracts into open-ended contracts for women and young people. These measures were continued by the Letta government, despite doubts concerning their cost efficiency, especially as regards their efficacy in creating additional jobs.¹⁵

12. It introduced a new system of unemployment insurance (*Assicurazione sociale per l'impiego*, ASpI) aimed at extending coverage to contractual typologies previously excluded. In fact, the reform fell far short of providing a universal measure of income support for those who had lost or never acquired the right to unemployment benefits. The law also aimed at strengthening the role of apprenticeship contracts as the main entry point to the labour market.
13. This part of the law also had a difficult start and was not taken up by firms to the expected extent. The length of time between renewals of fixed-term contracts was shortened (Law Decree 76/2013, 'Decreto Lavoro'); the restrictions on the number of times they could be renewed were relaxed (Law decree 34/2014); the legal limits on their length were extended (from 12 to 36 months); and regulation of the apprenticeship contract was simplified.
14. IRAP (Imposta Regionale sulle Attività Produttive) is a tax levied in proportion to turnover.
15. Empirical analysis has warned of the dubious efficacy of tax credit policies in creating additional jobs (see Cipollone and Guelfi 2002; Anastasia 2013). In fact, these policies do not create new jobs, but only attempt to redirect demand for labour towards more disadvantaged categories of workers. Despite several rounds of employment subsidies, the unemployment rate of young people aged 15–24 soared from a low of 20 per cent in 2007 to 39 per cent. This figure conceals large inequalities: in the South the unemployment rate is 50.5 per cent (and 56.1 per cent for young women).

Moreover, reductions of labour taxes – that is, ‘domestic devaluation’ – if implemented simultaneously by all countries, not only result in a zero-sum game, but, in recessionary conditions, are likely to trigger a deflationary process. The focus on youth employment was maintained in 2013, with 794 million euros (over three years) earmarked to subsidise employment stabilisation (Law Decree 76/2013 ‘Decreto Lavoro’). The Italian Plan on the Youth Guarantee for 2014–2020 is the first sign of a move towards a systemic approach to tackle youth unemployment based on improving education and training systems and facilitating transition from school to work.

Finally, the measures aimed at fostering productivity also relied primarily on tax rebates on the productivity bonuses negotiated at the second level of wage bargaining, as well as on ‘liberalisation’ measures.

Industrial relations: towards a new model?

In recent years there have been several attempts to weaken the trade unions by isolating CGIL, the main left-wing trade union confederation. In January 2009 a ‘separate’ agreement between two of the three main trade union confederations (not signed by FIOM-CGIL) and Confindustria (the Confederation of Italian Industry), with the backing of the government, refreshed the 1993 agreement and introduced new rules for wage indexation at the national level, while leaving to the second level (firm level) the distribution of productivity gains. In a round of negotiations at the plant level, Fiat imposed a new contract that introduced clauses that departed from the national contract. The bargaining on the new rules took place under emergency conditions and the threat of relocation (to Poland and Serbia). Once again the agreement was not signed by CGIL. In the heated debate that accompanied and followed the negotiations, Fiat opted out of the collective agreement by establishing a new company, to be known as ‘New Fiat’. The question is whether, under pressure of the global crisis, the new model of industrial relations successfully imported into Italy from the United States by Mr Marchionne – Fiat’s CEO – is likely to spread. Further efforts to increase flexibility by encouraging decentralised bargaining at firm/territorial level, and the possibility of derogating from the legislation on dismissals, were introduced by Law 148/2011 and reinforced by the Agreement on Productivity (November 2012), which extended to 2014 the tax exemption for productivity bonuses (enacted by the 2012 Budget Law), and broadened the

coverage of the second level of bargaining to include issues of work organisation, working-time, tasks and training (Fondazione Giacomo Brodolini 2014). The June 2011 inter-confederal agreement was signed by the three main trade union confederations. Although fiercely contested from within CGIL, this agreement paved the way to end CGIL's isolation.

The Italian welfare model

To conclude, the policies implemented in the crisis indicate a continuity with the philosophy inspiring the reforms implemented in the two previous decades in the areas of welfare and labour: cuts in social investment and social expenditure, privatisation, regressive taxation and pension reforms, labour market flexibility and weakening of national collective bargaining, scant recourse to active labour market policies and reliance on employment subsidies to cope with the surging unemployment of the weakest categories in the labour force. These policies have failed to achieve growth in the past (Zenezini 2014) and it is not clear how more of the same medicine in a time of deep crisis might produce different outcomes.

4. Effects of austerity and social policies

Six years into the crisis, the index of industrial production is still well below the level attained in 2007; productive capacity has shrunk by a quarter; consumption, investment and public spending have all dropped, with only the foreign component of demand showing some dynamism. While the fall in imports, combined with a rebound of exports, has brought the current account close to equilibrium, by reducing GDP and tax receipts, the crisis and the austerity policies have sent the debt/GDP ratio soaring above 130 per cent.

Employment conditions have dramatically worsened for all, but with very different outcomes because of the lack of universal relief measures: workers on typical contracts were initially shielded from unemployment through large-scale resort to the '*Cassa integrazione*' (Redundancy Fund); workers on temporary contracts – mainly young people of both sexes – and (male) immigrants endured labour shedding; and involuntary part-time soared in female employment.

Household impoverishment

Poverty indicators based on income and wealth summarise these developments well. The collapse in families' incomes and employment opportunities, and the lack of a universal safety net have resulted in an increase in poverty among lower income families and an impoverishment of the middle class. The share of Italian families in absolute poverty doubled between 2007 and 2012 (from 4.1 per cent to 8.0 per cent, with a sharp acceleration since 2011), with households with children, single parents and unemployed heads of family recording the sharpest increase (ISTAT 2014: 174). The share of severely deprived households (defined as families exhibiting four or more out of nine indicators of severe material deprivation) increased by more than 7 percentage points in three years (from 6.9 per cent in 2010 to 14.5 per cent in 2012). With widespread unemployment, pensioners are often the only ones left with a reliable source of income to support the family, while previously inactive women have been shoved into the labour market to supplement or make up for the loss of the male's income. While increases in the incidence of absolute poverty and material deprivation have been registered throughout Italy, they disproportionately affect households in the southern regions.

Policies to counter poverty and social exclusion are traditionally inefficient in comparative terms: social transfers are estimated to reduce relative poverty by only 20 per cent in Italy compared with 34 per cent for EU28 (ISTAT 2014: 177).¹⁶ Lacking a decent social protection system and a minimum income, worsening economic conditions and fiscal austerity measures call for a reinforced role for the family as income shock absorber, a role that it may increasingly find it difficult to maintain in the future. In fact, an increasing proportion of households have begun to deplete their savings. Moreover, the declining average size and changing composition of households – declining marriage and increasing divorce rates, increased number of single-parent families and the decline in fertility – might well have decreased their redistributive capabilities. Even so, with the welfare state being rolled back, traditional 'familism' is likely to remain Italian families' last resort. Insofar as income redistribution takes place inside the family, it is likely to favour increasing inequality and decreasing intergenerational mobility. Since families' main resource for absorbing external shocks (unemployment, disability, early retire-

16. According to Baldini *et al.* (2013) this poor result is due not so much to scant resources (17 billion euros in 2011) as to their inefficient use (see, for instance, footnote 11 above).

ment) is savings, which are very unequally distributed, reliance on families as insurers against social risk tends to reinforce social inequality.

Indeed, while rising inequality is a fairly general trend across the OECD countries, Italy has recorded the sharpest increase since 1992 and is now among the European countries with the highest inequality in income and wealth. The relative stability of the synthetic index of income inequality (Gini coefficient) conceals the multiple composition effects illustrated above. Income distribution has become more fragmented and unequal between and within social classes, among wage earners, across generations, between geographical locations and inside families. These multiple dimensions of inequalities have changed the relative position of social classes and have fragmented and split the social fabric: the malaise of the middle classes stems not only from their economic difficulties, but also from the disillusionment and frustration generated by uncertainty about their children's future and bleak labour prospects (Simonazzi and Villa 2010).

Macroeconomic consequences

At the height of the crisis, it was held that what set Italy apart from the other 'PIIGS' (Portugal, Italy, Ireland, Greece and Spain) was the financial security of Italian families. Still in 2009, it was estimated that the ratio of families' wealth, net of the public debt, to GDP was a remarkable 4.5. However, the length and depth of the crisis is eroding households' wealth,¹⁷ while overall inequality in wealth distribution is increasing: the richest 10 per cent own about 50 per cent of total wealth. Indebtedness as a share of income (still at very low levels compared with the EU average) also increased from 30.8 to 65 per cent between 2008 and 2012. The fall in disposable income caused the erosion of savings and a decline in the saving rate, concentrated on the lowest quintile, on households of young people and tenants. When considered in conjunction with the pension reform, this trend in young people's incomes and savings is suggestive of the problems that this generation will have to face in its old age.

As income volatility translates into a greater perceived insecurity, consumption is reduced and, as past savings are depleted, the prolongation of the downturn compels households to further cut consumption to at-

17. According to Bank of Italy's estimates, since 2008 households' wealth has diminished by 5.7 per cent (one-third of GDP).

tempt to safeguard the future.¹⁸ Insecurity helps explain the failure to boost growth of the only vaguely ‘pro-growth’ measure that the Renzi government has enacted, namely the 80-euro bonus given to low-wage workers. According to Confcommercio (a national association of retailers), Italian families were holding back from shopping ‘because their uncertainty about the future was stronger than the actual increase in funds in their pockets’. Inequality in income distribution is paralleled by polarisation in consumption: while the bottom 10 per cent accounts for only 4 per cent of total consumption, the top 10 per cent commands 22 per cent of it. The decline in the quantity of consumption has gone hand in hand with a quality downgrade: an increasing share of families declared that they had had to reduce either the quantity or the quality of their consumption relative to the previous year. This is the paradox of a productive system whose success has been based on the production of luxury goods (‘made in Italy’) that all too many Italians can no longer afford to consume: exports and imports of consumer goods increasingly differ in quality, imports being of much lower quality.¹⁹

5. What is to be done? The periphery and Europe

Macroeconomic effects of EMU

We can now see that, given the enormous distance separating the economic and political institutions of the Nordic-Continental countries from those of the European South, it was a mistake for the Mediterranean countries to enter a monetary union without a fiscal and political union. Survival of the weak in a currency union requires solidarity,²⁰ something that has never abounded within the European Community.²¹

18. Between 2007 and 2011 a 5 per cent reduction in GDP induced a fall in consumption of only 1 per cent; in 2012 the 2.4 per cent reduction in GDP was accompanied by a reduction in consumption of 4.3 per cent.

19. See Simonazzi, Ginzburg and Nocella (2013) for an analysis of the change in the pattern of consumption of poorer German families since the Hartz reform along these lines.

20. See the estimates of the federal transfers in the United States in *The Economist* (2011), or West German net transfers to the eastern *Länder*, estimated at about 900 billion euros between 1991 and 2003 (half of one year GDP) (Dustman *et al.* 2014).

21. It is now fashionable to say that economists have warned, since the very beginning, of the very demanding conditions required for a currency area to work properly. It is fair to say, however, that for a long time mainstream economists and politicians alike have let themselves be carried away by the ‘convergence play’, seriously underestimating the risks and costs inherent in wage and price flexibility as a prerequisite for convergence. See Simonazzi and Vianello (1998) for an early warning.

In the midst of the 'tsunami' that wrecked the financial markets, creating a panic among savers and inundating the sovereign debt and banking systems of half of the euro area countries, 'a controlled process of successive, agreed steps' was deemed the right answer. For too long the EU leaders, led by Angela Merkel, refused to acknowledge how interwoven national financial institutions had become. The leadership vacuum, lack of statesmanship and conflicting national interests have systematically prevented the timely adoption of the measures required to defuse the financial time bomb and that were later forced upon them by a new, ever deeper crisis. Even after her sweeping victory – or perhaps because of it – the German chancellor did not change course, however, turning down any call for greater integration or financial support for growth-enhancing projects, let alone requests to deviate temporarily from the budget targets because of exceptional circumstances (that the austerity measures helped to create).²² Finally, Germany's Constitutional Court has de facto undermined the only action that was capable of sedating the financial markets and preventing a domino effect on the whole financial system.

Solidarity is not only scarce, but also a very perishable good. Convergence, or at least self-sufficiency, must be perceived as attainable, sooner or later, and this demands that suitable policies be devised and implemented. The structural reforms implemented in the past few decades, and relentlessly requested by the ECB, the European Commission and Germany as a condition of assistance, are based on the premise that market competition is the only mechanism capable of guaranteeing growth. Innovation and successful enterprise supposedly are never the result of a coherent design, devised by an enlightened planner: it is the market that selects the most promising projects while letting the others fail along the road. This – it is argued – is the only way by which the Italian economy will break the vicious circle between public budget re-equilibration and recessionary fiscal consolidation, and this is what reforms should aim to achieve.²³ Thus, any failure to achieve the target can be ascribed to incomplete, half-hearted structural reforms: hence

22. The finance minister Pier Carlo Padoan's written request to the Commission on 16 April 2014 seeking authorisation for a change in objectives, due to severe recession, was greeted with dismay in Brussels and with outright rejection in Berlin. 'Italy request to push back budget targets dismays Brussels', *Financial Times*, 17 April 2014.

23. See '*Idee per la crescita*', a forum launched by a group of economists which aims at addressing the key question of how to stimulate and ensure sustainable growth in Italy on a liberal agenda. <http://www.eief.it/idee-per-la-crescita/>

the call for more labour flexibility, more spending and tax cuts, more deregulation and privatisations. The corollary is: the sooner, the better. Fiscal consolidation first, and no need to worry about the deflationary effects of balancing the budget (Perotti and Zingales 2011)²⁴; the belief is that austerity produces ‘confidence’ and confidence will produce growth. Implementation of ‘structural reforms’ at the national level is thus made a condition for the enactment of policies at the community level targeted at facilitating the financing of the deficit (quantitative easing) and/or coordinated growth. The devastation of the peripheral countries’ economies has barely dented this approach, nor convinced policymakers that, no matter how desirable and urgent some of these reforms may be, they are not, by themselves, capable of jumpstarting growth.

Italy’s (and other Southern European countries’) failure to achieve recovery is thus due more to these misguided policies than to delayed reforms. While there is agreement that some fundamental features are holding back growth and need to be fixed – the dysfunctional role of bureaucracy, the deterrent effect of high taxes (for those who pay them), the existence, within the public budget, of large pockets of privilege and waste, a political stalemate making bold reforms to clean out cronyism and corruption almost impossible – the main fault of this approach, and not a small one, is the idea that it will suffice to ‘unfetter entrepreneurship’ to restart growth. An alternative policy must be based on the tenet that aggregate demand must increase in order to create new job opportunities, and public (physical and human) infrastructure needs to be part of it. The tax base must be more equally spread and service provision must improve. This calls for a solution to the quandary of public employment and bureaucratic inefficiency. The concept of taxes must be connected again with the concept of services: people need to relearn that what they pay is for their health, education, child and elderly care. We need an industrial policy to identify the direction of development, guide investment, endeavour to ensure that the increase in demand does not leak out in imports and devise means to support the upgrading of value chains. New industrial relations and the revision of labour market

24. This position recalls Andrew Mellon’s advice: ‘liquidate labor, liquidate stocks, liquidate farmers, liquidate real estate ... it will purge the rottenness out of the system. High costs of living and high living will come down. People will work harder, live a more moral life. Values will be adjusted, and enterprising people will pick up from less competent people.’ Andrew W. Mellon, adviser to President Herbert Hoover during the Great Depression. Hoover, Herbert, *The Memoirs of Herbert Hoover*, Volume 3: *The Great Depression*. Herbert Hoover Presidential Library and Museum. www.hoover.nara.gov. Retrieved 20 August 2014.

deregulation are also needed, distinguishing between flexibility and insecurity. Indebted countries surely must do their homework, but we must reach an agreement on which 'structural reforms' are most needed. Moreover, structural reforms take time to achieve results and are best implemented in a context of growth.

Meanwhile, economic conditions have deteriorated rapidly: austerity is killing growth and the spectre of deflation is haunting Europe, the inevitable result of simultaneous, self-defeating demand suppression and wage cuts. With inflation low or even negative and low or negative growth, nominal GDP will hardly increase and may even contract, boosting the debt to GDP ratio. Ever larger primary budget surpluses would then be required simply to keep the debt to GDP ratio from rising further. According to IMF estimates (computed with reference to the more favourable conditions prevailing in 2013), the heavily indebted European sovereigns should run an average primary surplus: 5.6 per cent for Ireland, 6.6 per cent for Italy, 5.9 per cent for Portugal, 4.0 per cent for Spain and 7.2 per cent for Greece in the decade 2020–2030 in order to first stabilise and then reduce their debt/GDP ratios to the 60 per cent level targeted by the EU's Fiscal Compact by 2030 (IMF 2013). Drawing on historical experience, Eichengreen and Panizza (2014) doubt that these large primary surpluses can be politically and economically acceptable and, we might add, successful. Italy has in fact run a primary surplus since the early 1990s, but that did not stop the weight of the debt from climbing. Moreover, history teaches us that the consequences of a general deflation can be disastrous.

Europe must resume growth if the countries of the periphery are to have a chance of growing out of their debt. But the situation has so deteriorated that growth alone will not suffice to defuse the time bomb represented by deflation and the debt overhang, calling for some sort of financial relief. This inevitably calls into question Germany's policies and attitude.

The grumbling hive

The survival of the common currency very much depends on the existence of a common interest linking surplus and deficit countries and capable of supporting a commonality of policies: a political entity that takes care of Europe. But interests within Europe are diverging. In 2011 George Soros expressed the view that 'with Germany's reunification, the

main impetus behind the integration process was removed' (Soros 2011). The impetus might have been weakened further by the crisis. The economic crisis and fiscal austerity have depleted the Southern European markets. They are no longer as important to Germany as the more dynamic extra-EU markets;²⁵ the eastward integration of German industry has provided a cheap, skilled workforce and an increasingly interwoven network of suppliers and markets. Despite an increase in German wages since 2009 (see the chapter on Germany in the present book), there are two reasons to expect any beneficial effect for the southern countries to be modest: first, the rate of Germany's domestic demand expansion is still very low and second, its spillover effects within the euro zone are likely to be smaller because of the increasing importance gained by non-euro countries in German imports of consumption goods. Thus, even somewhat stronger and more balanced growth in Germany could not outweigh the disastrous impacts of austerity and of deregulatory EU policy approaches (see the chapters by Leschke *et al.* and Schulten/Müller in this volume).

External policies are also likely to diverge: what is good for Germany is not necessarily good for the weaker countries of the European Union. German industry's conquest of new emerging markets may require a more liberal trade policy than one that the southern European countries can afford.²⁶ The domestic industries of the latter will have to face competition in their own markets, competition made stiffer by the impoverishment of families. Moreover, without Germany, the euro would be weaker. A strong euro can harm Germany less, because of the composition of its exports and the positive effects that a strong balance and a strong euro may have on the price of imported consumption goods and on the capacity to finance exports, as argued above. Conversely, a strong euro can harm the Southern countries, whose exports are likely to have a higher price elasticity. Finally, the trade surplus entails bottom-low interest rates in Germany, which gives German firms the privilege of low credit costs compared with those paid by firms in other countries, as well as low rates on long-term financing offered to foreign buyers of investment goods. Thus, the 'spread' in interest rates signals two sides of the

25. Between 2008 and 2012 German exports to Italy, Spain and Greece fell by 10 per cent, 27 per cent and 40 per cent, respectively.

26. Conflicting interests – between big business and labour, as well as between countries – may also unravel the Transatlantic Trade and Investment Partnership (TTIP), a comprehensive free trade and investment treaty currently being negotiated between the European Union and the United States.

same coin when it comes to understanding the German business model and its side-effects on the economies of other advanced capitalist countries within the euro zone, such as Italy.

Can Germany stand alone? For German voters, their country's post-war economic miracle was built on a hard currency, prudent finances and strong exports. It is hard for German voters to fathom that – unintended consequences of – these very virtues are at the heart of the current crisis (Knight 2011). As noted by former UK prime minister Gordon Brown, 'There is some truth in the argument that Germany will only agree to become a bigger part of the solution when faced with the evidence that it is also a big part of the problem' (Brown 2011). Emergency intervention is needed to pave the way for long-term construction: this is a growth strategy that would mean easing up on austerity for the weakened countries of the periphery and enacting strategic investment stimulus measures in both periphery and surplus countries, emergency measures to cope with the debt overhang, as well as new rules that prevent the formation of the very disequilibria that led to the present predicament. This would be a bitter pill to swallow for the German electorate and their political class. There has been little so far to encourage hope.²⁷

Time is running out fast and it will become more and more difficult to ensure the sustainability of peripheral countries' debt. We may have reached a point at which not even a compliant Germany would be able to pay the bill for everyone and, if deflation continues, the alternative scenario can no longer be ruled out. As Barack Obama has said, European leaders' lack of vision and resolve is scaring the world.

27. During the spring the *Financial Times* published details of a document jointly issued by the German and Finnish finance ministries which strongly rebuked Brussels for easing austerity demands, citing in particular the additional flexibility given to France and Spain for reducing their budgets to within EU deficit limits (Hugh 2014).

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Greece as an international test-case: economic adjustment through a Troika/state-induced depression and social catastrophe

Maria Karamessini

1. Introduction

The sovereign debt crisis that started in 2009 marks the demise of the Greek socio-economic development model, which had produced high growth rates and productivity gains over the period 1994–2008. The causes of the Greek sovereign debt crisis are undoubtedly structural and mainly internal, but one should not neglect the links between Greece's sovereign debt, on one hand, and mass lending by European banks and the functioning of unregulated global financial markets, on the other. Last but not least, the Greek sovereign debt crisis would not have erupted if the global financial crisis – which revealed the limits of the financialisation of advanced capitalist economies – had not occurred and if the Economic and Monetary Union (EMU) were more solidaristic and less neoliberal, which would, among other things, make possible a bail-out clause for EMU member states in the EU Treaty and the recognition of the European Central Bank (ECB) as a lender of last resort.

In 2010 and 2012 Greece received financial assistance of historic dimensions from its euro-zone partners and the IMF. However, this assistance does not reflect solidarity between partners or on the part of the international community. Preventing disorderly default by Greece, the main aim of the first loan package granted in mid-2010, was intended to save the euro zone and European and American banks from collapse and to preserve the stability of the international financial system. A lack of solidarity is also evident in subsequent sovereign debt management policies. The second euro zone/IMF loan package was adopted at the beginning of 2012. It accompanied a 53.5 per cent 'haircut' on sovereign debt held by private sector investors. New loans were used to repay sovereign debt coming to maturity and cover the costs of the private-sector-investor operation and the required recapitalisation of Greek banks.

Last but not least, the disbursement of external loans was made conditional on the strict implementation of two Economic Adjustment Programmes supervised by the ‘Troika’ (European Commission, ECB and IMF). These were supposed to accelerate and complete the neoliberal project in Greece, which was considered as a laggard in the EU in this respect, and to recast the country’s growth pattern and social model. The outcomes of the implementation of the two Economic Adjustment Programmes include a deep and prolonged recession, historic levels of unemployment and poverty and a huge destruction of productive capacity, which have dumped the economy in an austerity trap and a debt trap.

It is important to underline that, since 2010, Greece has become an international test-case – an experiment *in vivo* – for the effectiveness of the neoliberal project as an exit strategy from a structural crisis in an over-indebted country that is a member of a monetary union and thus unable to use such tools as printing money or devaluating its currency in order to repay sovereign debt and redress the current account deficit. The Greek economic adjustment experience is not only testing the feasibility of ambitious economic policy targets in a tight time schedule – that is, fiscal consolidation equal to 21.4 per cent of GDP and a 20 per cent devaluation of wages and prices – but also testing the social and political sustainability of state-led depression and ‘structural adjustment’ that are not only depriving huge numbers of the working-age population of employment, but are also sweeping away social rights and the welfare state and shrinking the role of the state, small entrepreneurs and independent workers in economic activity.

In this chapter we discuss the economic and social effects of the neoliberal response to the Greek sovereign debt crisis and focus in particular on the changes it implies for the pre-crisis socio-economic model. In Section 2 we briefly describe this model and in Section 3 examine its initial success and the vulnerabilities that led to its collapse in the face of the global financial crisis. Section 4 analyses the rationale, objectives and measures of the Economic Adjustment Programme and its contribution to the dismantling of the socio-economic and employment models. Section 5 demonstrates the disastrous implications of the policy recipe implemented. We conclude with a discussion of prospects and alternatives.

2. A socio-economic model in transition from state-led to liberal capitalism (1994–2008)

The period 1994–2008 can be characterised as one of difficult transition from a state-led familistic to a liberal, partly de-familialised capitalism in Greece (Karamessini 2009). In this section we describe the basic elements of the growth model and changes in the production and welfare regimes and the employment model in these years.

2.1 Growth model and macroeconomic policy

After a long period of economic crisis in the 1980s and early 1990s, in 1994 the Greek economy entered a period of sustained growth which ended with the global financial crisis in 2008. During 1994–2007 GDP grew annually by 3.7 per cent on average; indeed, from 2001 to 2007, the Greek economy was the fastest growing economy in the euro zone, after Ireland. High rates of investment and productivity growth prevailed over the whole period but job creation was insufficient to absorb both new labour force entrants and heavy immigration inflows during 1994–1999. The unemployment rate thus increased by 3.3 percentage points between 1993 and 1999 and declined only in the following decade (from 12.1 per cent in 1999 to 7.7 per cent in 2008).

Rising domestic demand and profitability were the main drivers of private capital accumulation and GDP growth. The main determinant of increase in domestic demand was consumption, fuelled by rising real wages, rents and profits, and sustained public spending, tax cuts and tax evasion, and growing private borrowing. A second determinant was public investment in infrastructure – which accelerated in the years before the 2004 Athens Olympics – and private residential investment. As for profitability, the other driver of private capital accumulation, this followed a steady upward trend over the whole period. In 2007, the profit rate was only 7 per cent below its average in the ‘golden’ post-war period of Greek capitalism (1961–1973).

During 1994–1999, macroeconomic policy was geared towards preparing Greece for joining the Economic and Monetary Union (EMU). It consisted of restrictive fiscal and exchange rate policies and interest rate reductions. Restrictive fiscal policy and the continuation of the policy of drachma overvaluation, initiated in 1987, contributed to a marked

decrease in inflation, the public deficit and the debt-to-GDP ratio, but also to a major deterioration in competitiveness, although falling interest rates stimulated productive investments. Greece joined EMU on 1 January 2001 and benefited from the euro's low interest rates. Real interest rates were even lower because Greece maintained a permanent inflation differential with the euro area.

Fiscal policy became strongly expansionary in the first half of the 2000s, breaching the 3 per cent limit for public deficits in EMU. The public deficit escalated from 3.1 per cent to 7.5 per cent of GDP between 1999 and 2004. Although some effort was made towards fiscal adjustment in 2005, the public deficit rose again, to 6.4 per cent of GDP in 2007. The gross public debt-to-GDP ratio also followed an upward trend; it passed from 96.3 per cent in 1994 to 98.9 per cent in 2004 and 105.4 per cent in 2007. Falling interest rates from 1994 to 2000 and very low real interest rates from 2001 onwards provided a strong incentive for both public and private borrowing. Savings fell from 20.4 per cent of GDP in 1994 to 7.1 per cent of GDP in 2008, while Greek household debt reached 45.3 per cent of GDP in 2007 (Bank of Greece 2008). Expansionary fiscal policy and low interest rates fuelled domestic consumption and investment and kept inflation constantly above the euro zone average by 1–1.5 percentage points, thus undermining competitiveness, while the huge drop in savings below investment increased external debt and current account deficits (Economou 2010).

2.2 Production system and regime

At the end of the 1980s Greece was the most agrarian and second-least tertiarised economy in the EEC, after Portugal; the share of public sector enterprises in GDP was the third highest in Western Europe after those of Portugal and Italy; product market regulation was among the strongest in the OECD; and micro and family enterprises thrived in both the agricultural and non-agricultural sectors.

In the 1990s and 2000s, the importance of agriculture and manufacturing in GDP continued to decline, as in the 1980s, while production and growth dynamics moved decisively towards tourism, construction, services and shipping. At the same time, major transformations took place in the production regime, namely the privatisation of state-controlled banks and public companies, contracting-out of public activities

to private firms, market deregulation in banking and public utilities and capital concentration in private services. Although important by Greek standards, the privatisation and market deregulation processes were slow by international comparison and partial in many cases because of strong resistance by unions and public opinion, especially to the privatisation of public utilities. European capital was a major actor in these developments. European industrial firms and multinationals bought out industrial firms, carried out the most important public works in consortiums with Greek firms, took over big public procurement contracts, participated in privatisations of public companies and invested in retail, banking and insurance, telecoms and hotels to take advantage of the rapidly growing demand for services.

The aforementioned changes in the production system and regime further increased the feminisation of employment and were accompanied by extensive use of migrant labour to cover labour shortages and reduce labour costs in many sectors. Migrants today constitute the majority of manual workers in Greece.

2.3 Welfare state and regime

The main characteristics of the Greek welfare state and regime at the end of the 1980s were as follows (Karamessini 2010):

- an extremely fragmented pay-as-you-go pension system with major inequalities in entitlements, a diminishing ratio of insured persons to pensioners and extensive and long-standing contribution evasion;
- major disparities in levels of cover and access to health care between different population groups and a high level of private health expenditure despite the newly established National Health System (NHS);
- strong familialism and gender bias, reflected in the residual character of unemployment compensation, social assistance and social care systems, as well as in the lower statutory age of retirement for women and special early retirement schemes for married women and mothers of children under 18. Strong familialism and the gender bias of the welfare regime kept the female activity rate low.

Reforms of the pension system in the 1990s and 2000s established mixed funding of insurance funds through contributions and general taxation. They also introduced a means-tested supplement to low basic pensions, increased the minimum insured time for full pension entitlement and reduced the replacement rate of pensions. Furthermore, they gradually equalised the legal age of retirement between public and private sector employees, tightened the eligibility criteria for early retirement of women with minor or disabled children and equalised women's statutory retirement age with that of men at 65 for those insured after 1 January 1993. However, the reforms did not ensure the financial sustainability of the pension system, which has been eroded primarily by extensive contribution evasion on the part of employers and the expansion of informal employment. Similarly, reforms of the public health service have not prevented the spectacular rise in private health expenditure, which reached 57 per cent of total health expenditure in 2005, the highest share among OECD countries.

The late 1990s and 2000s also saw an improvement in the terms of maternal and parental leave and the proliferation of child and elderly care services. However, this active reconciliation policy came fairly late relative to the growing demand for care by dual-earner households. The gap was covered by large numbers of migrant women hired by high- or medium-income households as carers for children and the elderly. Just before the current crisis, Greece had the lowest coverage of children and elderly by care services in the EU15. Such low coverage, along with very high youth unemployment rates since the early 1990s, were the main determinants of the significant fall in the fertility rate and entrapment in low-fertility equilibrium.

2.4 Industrial relations and wage determination

From the mid-1970s through the 1980s industrial relations were extremely conflictual, while state intervention in wage determination was very strong. The 1990s and 2000s saw a weakening in such intervention and a decrease in capital–labour conflict. In 1990, the system of automatic indexation of wages to inflation was abolished, while a new law on ‘free collective bargaining’ changed its structure and replaced state-controlled compulsory arbitration – in place since 1955 – with independent third-party mediation and arbitration. As a result, the share of arbitration awards in the total number of collective agreements declined

sharply. Strike activity also declined in the 1990s. The recession of 1990–1993, the ideological impact of the collapse of the communist bloc on the union factions of the Left and the accession to power of a liberal government that remained in office during 1990–1993 contributed to a turn by the majority of trade unionists towards a social-partnership approach to industrial relations, away from the adversarial approach of the previous period (Karamessini 2009). EU integration is an additional determinant of the gradual decline in industrial relations conflict. Its influence has been exerted through the establishment of social dialogue institutions and the achievement of social consensus on Greece's accession to EMU, which persuaded trade unions to moderate wage claims (Kouzis 2002).

National-level bargaining on the national minimum wage and sectoral or occupational minima is a core feature of the Greek collective bargaining system. Company-level agreements are relatively few in number. Outside the public sector, the basic pillar of the Greek union movement in the 1990s and 2000s was public utilities and banking, which also dominated the leadership of the National Confederation of Greek Labour (GSEE) throughout this period. Because of high union density, employment protection and their capacity to mobilise their members, public utility and banking unions were equally the basic pillar of general strikes, which reinforced GSEE's bargaining power during negotiations on the National General Collective Agreement. The role of the latter is crucial in the collective bargaining system, because it not only determines the level of the national minimum wage but also sets the floor for employment and working conditions and workers' rights (working time, leave, rights of part-timers, apprentices, student workers, equal treatment, funding of training, severance pay and so on). Since the 1980s, in bargaining with employers' organisations, the union federations of private sector employees have used national minimum wage increases as the floor and the best rate achieved by public utilities and banking federations as the target. In the late 1990s, the bargaining rounds between management and the strong unions in public utilities and banking were decoupled from those between GSEE and peak employers' organisations on the national minimum wage. A basic mechanism of articulated bargaining and wage drift was thus broken (Ioannou 2000).

Real compensation per employee declined substantially during 1990–1993 (3.2 per cent per year on average) and then increased slightly below productivity between 1994 and 2000. Although the position of employers' organisations in wage bargaining became harder in the EMU

context (Ioannou 2010), real wages increased slightly above productivity between 2001 and 2007.

2.5 Employment regime

Strong protection of formally employed permanent employees against dismissal, especially white-collar workers, has been a core element of the traditional Greek employment regime, along with extensive informal/irregular employment. The former has remained intact for the past twenty years, the only exception being a 2005 law that abolished for persons newly hired in public utilities the stronger protection against dismissal of employees in these firms than in private firms. As for informal employment, this expanded in the 1990s and 2000s, mainly due to mass illegal immigration and the irregular situation of large numbers of migrants staying and working in Greece. However, efforts have also been made to introduce types of formal employment and working time flexibility in the labour market in the past twenty years. Union opposition tempered the level of flexibility introduced by governments, however, and ensured relatively good protection for employees involved in some forms of atypical work, such as part-timers and temporary agency workers. In 2007, Greece had the lowest rate of part-time employment and incidence of flexible working-time arrangements in the EU15, while the rate of fixed-term contracts among employees was below the EU27 average. At the same time, project/service contracts among dependent workers, uninsured employment and informal/irregular work thrived but, by their very nature, remained unrecorded.

3. From success to collapse

The socio-economic model just described achieved very high GDP and productivity growth over the whole period of 1994–2008, leading to real economic convergence with more developed EU economies. Other successes of the model were: real wage growth in line with productivity, which allowed workers to reap the fruits of growth; great stability of employment for permanent employees; and a continuous rise in the female employment rate. But the model also suffered from shortcomings, such as low job growth, high youth and female unemployment rates, pronounced labour market segmentation, precariousness in the legal status and living conditions of migrants, high income inequalities and poverty

rates – primarily due to the inadequately redistributive character of the tax and benefit system – and a rapidly rising current account deficit. However, it is the high indebtedness of the state that proved to be the model's Achilles heel.

3.1 Growing current account deficit

The current account deficit climbed from 3.2 per cent of GDP in 1998 to 16.3 per cent in 2008, while the deficit of the balance of goods and services rose from around 10 per cent in 1998 to 12.7 per cent of GDP in 2008. The balance of goods and services was responsible for only 31 per cent of current account deficit deterioration between 1998 and 2008, however, the remainder accounted for by the incomes balance – a major increase in interest payments for external debt – and the decrease in net current transfers (Manassaki *et al.* 2010).¹ Regardless of each component's contribution to the deterioration of the current account deficit, it is evident that the huge deficit of the balance of goods and services is no longer sustainable from a longer term growth perspective. The question is what its determinants are. Debate on this topic is highly controversial.

Throughout the 2000s, the Bank of Greece has attributed growing deficits in the balance of goods and services mainly to losses in price competitiveness due to the persistent inflation differential with the euro zone average. Indeed, between 2000 and 2008 Greece's real effective exchange rate based on consumer prices appreciated by 8.1 per cent in respect of the other euro zone partners and by 17 per cent in respect of all trading partners. But as early as 2003, the Annual Report of the Governor of the Bank of Greece suggested that real wages should increase less than productivity, while nominal wages should increase in line with productivity and average inflation in the euro zone until the inflation differential was erased. Asking wage earners to bear the full adjustment cost followed the mainstream approach of EU institutions. Wage-driven inflation was later contradicted by EU publications attributing 67 per cent of the rises in Greek prices during the first half of the 2000s to profit margin increases, 20 per cent to indirect tax increases and 13 per cent to labour-cost increases (ECB 2006; European Commission 2007). Given

1. Transfers to Greece include emigrants' remittances and EU transfers within the framework of the Common Agricultural Policy, while transfers from Greece include immigrants' remittances and the country's contributions to the EU budget.

that real wages grew in line with productivity during that period, the finding that inflation was mainly profit- and tax-driven was very important with regard to assigning responsibilities to the actors involved in determining the outcome. Alternatively, the Annual Reports and several studies by the Institute of Labour of Greek Trade Unions (see, for instance, INE GSEE/ADEDY 2010; Ioakimoglou 2011) have repeatedly underlined the minimal role played by labour costs in the loss of competitiveness in the 2000s; highlighted the important role played by euro appreciation² – 36 per cent between 2001 and 2008 – and low non-price and structural competitiveness; and showed that Greek employers could easily have increased price competitiveness by reducing their profit margins, given that these were the second highest in the EU15 after those in Ireland during 1995–2009. These reports and studies, finally, attributed a significant part of deficit deterioration not to loss of competitiveness but to the much higher growth in Greece relative to its trading partners.

Empirical evidence corroborates the minimal role of labour costs in explaining the deterioration in the balance of goods and services between 1998 and 2008. However, analyses of all the aforementioned institutions have missed the important fact that 38 per cent of the deterioration was due to the fuel-related deficit, caused by the significant rise in petrol prices and Greece's great energy dependency on petrol.

3.2 High sovereign debt

As already mentioned, the gross public debt-to-GDP ratio rose from 96.3 per cent in 1994 to 105.4 per cent in 2007, despite falling interest rates in the process of joining EMU, low interest rates after adopting the euro in 2001 and high GDP growth throughout the period 1994–2007. High GDP growth and profit rates induced European banks to lend abundantly to Greek firms, banks and the state (Milios and Sotiropoulos 2010). In a situation of oversupply of funds and low interest rates, the Greek sovereign debt not only seemed but was indeed refundable and repayable.

High public indebtedness at the onset of the global financial crisis represented the cumulative effect of a long-standing public revenue defi-

2. Greece's extra-Eurozone trade represented about 40 per cent of exports and 45 per cent of imports in 2007.

cit (Stathakis 2010). In 2006, total public revenues were equal to 39.2 per cent of GDP (against 44.6 per cent for the EU27), while total public expenditure was 45.1 per cent of GDP (against 46.2 per cent for the EU27). This deficit stemmed from structural tax avoidance and evasion by firms and the self-employed; tax privileges of banks, maritime capital, the Church of Greece, liberal professions and so on; as well as tax concessions for capital and high incomes since 2000. As a result, direct taxes decreased from 9.7 per cent of GDP in 2000 to 8.2 per cent in 2007, while indirect taxes fell from 13.8 to 12.7 per cent of GDP across the same period. With regard to tax evasion, it is indicative that 64 per cent of all Greek taxpayers declared income below the tax-free income ceiling and 17 per cent zero income for 2008, while wage earners and retirees paid 63 per cent of all income tax for the same year (Vasardani 2011). On the expenditure side, the sovereign debt reflected the cumulative effect of excessive military expenditure; the cost of rescuing indebted private firms in the 1980s and, recently, banks; extensive corruption of public officials leading to overpricing of public works and public procurement; the deficit of the 2004 Athens Olympics; and growing social security deficits financed by the state budget: 6.6 per cent of GDP in 2009. Estimates of military expenditure indicate that Greece annually spent 5.8 per cent of GDP on armaments in the 1970s, 6.2 per cent in the 1980s, 4.6 per cent in the 1990s and 3.1 per cent during 2000–2008 (Grebe and Sommer 2010). As for corruption, this should be regarded as an essential component of the economic model rather than an obstacle to a liberal economy (Laskos and Tsakalotos 2013), encouraged by contracting-out of public works and activities and big public procurement projects.

Although the structural determinants of Greece's high sovereign debt are internal, Greece is also paying for a global crisis it did not provoke and the deficiencies of EU integration, in respect of which it was not the only and certainly not the main responsible party. In other words, without the global financial crisis, the Greek sovereign debt crisis would not have erupted, while the skyrocketing of the debt due to speculation would have been stemmed if the EU Treaty on EMU did not exclude the bail out of a member state by its partners in case of financial difficulty. Moreover, in a more solidaristic common currency area in which the ECB was the lender of last resort, the restructuring and refinancing of Greece's sovereign debt would not endanger its foundations.

3.3 Collapse and conditional 'rescue'

The global financial crisis turned a high but manageable debt into an uncontrollable and unsustainable one. As a result of a strongly counter-cyclical fiscal policy implemented in 2008 and 2009, the public deficit passed from 6.5 per cent to 15.7 per cent of GDP and the gross sovereign debt from 107.3 per cent to 129.7 per cent of GDP between 2007 and 2009. Financial market speculation on Greece's sovereign bonds started in mid-November 2009, in an international context of rising sovereign debts and short supply of global financial capital, looking for the most secure financial investments internationally. Questioning the solvency of the Greek state and betting that the EU would not bail out Greece, financial market investors pushed upwards spreads on Greek sovereign bonds and the price of credit default swaps.

In response to its EU commitments (European Council, Euro Group and ECOFIN decisions) and to soothe financial markets, between December 2009 and March 2010 the Greek government announced four packages of measures meant to reduce the public deficit. Despite the adoption of these packages, speculation in financial markets soared and Greek sovereign bond spreads skyrocketed. As a result, the Greek government requested financial assistance from the euro area. Greece's default would not only entail the collapse of its major lenders – mainly French and German banks – but also sweep away EMU. In 2 May 2010, the Greek government, the European Commission, the European Central Bank (ECB) and the IMF agreed on an economic adjustment programme (EAP) in exchange for financial aid provided by euro-zone countries and the IMF (European Commission 2010). Support would be provided by instalments whose disbursement was conditional on the strict implementation of a Memorandum of Understanding (MoU 1), describing in detail the measures to be taken by the Greek government and revised periodically.

One year after the implementation of the Economic Adjustment Programme and despite a considerable reduction of the public deficit in 2010, recession led to substantial deviations from fiscal adjustment targets for 2011, a spectacular increase in the sovereign debt-to-GDP ratio and Greece becoming unable to service its debt. At the same time, financial market speculators were attacking Italy's and Spain's sovereign bonds. On 21 July 2011, euro-area country leaders decided a second financial aid package for Greece with lower interest rates and extended

maturities for new loans to be disbursed by the European Financial Stability Facility (EFSF). For the first time, private lenders were urged to participate voluntarily in the whole package of debt refinancing/restructuring. In exchange for this second financial bailout, the Greek parliament adopted, by a slim majority, a Medium-Term Fiscal Strategy 2012–2015 (MTFS), prolonging and reinforcing the austerity measures and structural reforms of the Economic Adjustment Programme and adding a huge privatisation programme of public firms, agencies and assets. By October 2011, the debt-to-GDP ratio soared due to the huge interest-rate-to-growth differential. On 26 October, the Euro summit recognized that voluntary roll-overs of existing Greek debt at maturity by private investors did not allow a substantial reduction of the required funding within the new fiscal adjustment programme and did not protect against selective default. This is why it decided a 50 per cent nominal discount on notional Greek debt held by private investors.

The concrete offer to private lenders to encourage their involvement in the process of debt restructuring (PSI), as well as the amount and usage of the new loans to be provided by euro-zone countries and the IMF (financing of new bonds, recapitalisation of the Greek banking system, coverage of 2012 primary deficit) were finally decided by the Euro group on 21 February 2012. The new financial aid package was made conditional on the implementation of a second (revised) Economic Adjustment Programme accompanied by a new Memorandum of Understanding (MoU 2) setting the economic policy conditionality.

In spring 2012, continued political instability led to elections that created a very tense environment, in which uncertainty about the outcome of a second election led to mass capital outflows. The 17 June election resulted in the formation of a coalition government with the mandate to continue implementation of the revised Economic Adjustment Programme.

Taking into account the delay in the implementation of the EAP and action taken by the new government on 26–27 November 2012, the euro area finance ministers and the IMF agreed to extend the fiscal adjustment path by two years, involving a reduction of the primary surplus target for 2014 to 1.5 per cent of GDP and an even annual adjustment until a primary surplus of 4.5 per cent of GDP is achieved in 2016. They also agreed on a package of measures aimed at reducing Greece's debt by 2020. In parallel, Greece proceeded to a debt buy-back operation through public debt tender purchases.

4. Supervised economic adjustment and acceleration of the neoliberal project

Apart from saving the euro and EMU, the voluminous financial aid provided to Greece by the euro-zone countries and the IMF and EAP served the interests of Greece's creditors, as well as those of the hegemonic sections of Greek capital owners. They were intended to prevent losses on the part of the European and American banks holding Greek sovereign bonds and to satisfy long-standing demands made by the Confederation of Greek Enterprises, which welcomed the Economic Adjustment Programme as an opportunity to suppress social resistance to 'necessary reforms'. EAP is a neoliberal project in which 'adjustment' is sought through a massive assault on workers' incomes and rights, public ownership and the welfare state. In this way, it accelerates and completes the transition of Greece's traditional model of state-led capitalism to a liberal model of capitalism under the auspices of its lenders. Financial aid conditionality and its supervision by the Troika (ECB, European Commission and IMF) have entailed a substantial loss in national sovereignty with regard to economic and social policymaking, as well as a host of infringements of the Greek Constitution.

4.1 Neoliberal offensive, 'shock therapy' and the punitive character of financial aid

The EAPs endorsed the 'Washington Consensus' which epitomises the neoliberal project worldwide and inspired the IMF Structural Adjustment Programmes in developing countries. There were three basic objectives: (i) fiscal consolidation to create primary surpluses in the general government balance and curb increases in sovereign debt; (ii) stability of the banking system through liquidity guarantees, given the high exposure of Greek banks to Greek sovereign bonds; and (iii) 'internal devaluation' to improve competitiveness and reduce external deficits. The term 'internal devaluation' is synonymous with reductions in labour costs, given that national currency devaluation is impossible. Finally, by reducing consumption and encouraging private investment through austerity measures, internal devaluation, public sector downsizing and privatisation, the EAPs were intended to push the Greek economy towards a private-investment and export-led growth pattern. No reference was made in either of them to technological progress, innovation and structural competitiveness.

Table 1 Government balance and sovereign debt, Greece (% of GDP)

	General balance		Primary balance		Sovereign debt
	1st EAP targets	Achieved	1st EAP targets	Achieved	Achieved
2009 base year	-13.6	-15.7	-8.6	-10.5	129.7
2010	-8.0	-10.9	-2.4	-5.1	148.3
2011	-7.6	-9.6	-1.0	-2.4	170.3
2012	-6.5	-8.9	1.0	-3.9	157.2
2013	-4.9	-12.7	3.2	-8.7	175.1
2014 end year	-2.6	-1.6*	5.9	2.8*	177.2*

Note: * Forecasts.

Sources: EAP (2010) for first and third columns; European Commission (2014) for second and fourth columns.

Besides its neoliberal character, a crucial trait of the first EAP was its ‘shock therapy’ approach to fiscal adjustment. A huge frontloaded fiscal consolidation effort was carried out during the first year and a half of the programme. As a result, the primary government deficit was reduced from 10.5 per cent in 2009 to 2.4 per cent in 2011. Despite this remarkable outcome, the EAP target of creating primary fiscal surpluses from 2012 onward in order to start repaying creditors was not achieved due to a revision of the deficit for the base year and the great recessionary impact of the ‘shock therapy’, officially not anticipated by the Troika and the macroeconomic model used for the EAP. On the basis of ex-post evidence, the IMF economists Blanchard and Leigh (2013) and later the IMF itself recognised that fiscal multipliers of the macroeconomic model used for Greece were seriously underestimated. However, it is equally likely that the Troika set unrealistic fiscal targets in the initial EAP on purpose, to maintain permanent pressure on the Greek government to achieve compliance with economic policy conditionality.

In structural terms, the fiscal adjustment is estimated at nearly 14 percentage points of GDP between 2009 and 2012, while the planned fiscal adjustment for the next two years amounted to 7.3 per cent of GDP in 2013–2014 (OECD 2013: 17–19).

The preference on the part of creditors for a huge and frontloaded fiscal consolidation regardless of the strong recessionary shock that this

would produce and the initially high interest rate incurred for euro-zone country loans (5.2 per cent) reflect the punitive character of the initial loan package granted to Greece by euro-zone partners in 2010. Additionally, the strong recessionary shock was functional to the achievement of internal devaluation, the second objective of the EAP. The ensuing rise in unemployment was expected to curb workers' resistance to wage reductions and withdrawals of employee rights, classified by the EAP's authors as 'labour market rigidities' that obstruct the reduction of labour costs. After a 1.7 per cent fall of private sector nominal wages in 2011, reducing nominal unit labour costs in the business sector by 15 per cent in 2012–2014 became an explicit target of the second EAP, adopted in February 2012. Reducing such costs was considered as key to the internal devaluation, which was intended to restore competitiveness through the transmission of labour-cost reductions to prices.

4.2 Fiscal consolidation, public sector downsizing and welfare state retrenchment

According to the EAPs, fiscal consolidation is to be attained through restrictive fiscal policy and structural reforms. Public expenditure was reduced by 29.7 per cent between 2009 and 2013, while public spending cuts contributed 58.6 per cent to overall fiscal consolidation through 2010–2013 (Anderson 2013). The expenditure-reducing measures of the EAPs have not and do not only serve fiscal consolidation purposes but also a broader political/policy goal: the reduction of the size and role of the public sector in economic activity and welfare provision.

Austerity measures to reduce public spending

Austerity measures implemented since the beginning of 2010 include major cuts in the following: wages, bonuses and overtime payments in the public sector; public and private sector pensions; operating expenditures of line ministries; state budget allocations to municipalities and social security agencies; and public investment.

The first EAP and Medium-Term Fiscal Strategy (MTFS) 2012–2015 aimed explicitly to bring the public sector wage bill down from 13 per cent of GDP in 2009 to 8.1 per cent of GDP in 2015 and to reduce the 11 per cent wage premium of the public sector over the private sector, after controlling for employee and job characteristics. Between May 2010 and

May 2011, nominal wages in the civil service decreased by 15 per cent and those in public utilities, agencies and undertakings by 25 per cent, while nominal pensions in the public and private sectors fell by 10 per cent. The respective declines in real wages were 20.4 per cent and 30.4 per cent, while real pensions fell by 15.4 per cent. Additionally, a new single pay scale in public administration took effect on 1 November 2011, bringing about a new reduction in civil servants' nominal wages by 17 per cent per cent, on average (IMF estimates cited by Tzannatos and Monogios 2012). Wages in public utilities and undertakings were subject to cuts of similar magnitude, which took effect on the same date. Finally, a reform of the special wage regimes (judges, diplomats, doctors, academics and so on), which account for about one-third of the public sector wage bill, took effect on 1 August 2012, resulting in 20–30 per cent wage reductions, on average.

Reduction of the public sector wage bill also requires retrenchment of public employment. A series of measures were implemented towards this end:

- Increase in standard working time from 37.5 to 40 hours a week without any rise in pay and a drastic reduction in overtime working.
- Suspension of recruitment of permanent employees in the public sector in 2010, except in education, health care and security; application of the rule 'one hire for 10 exits' in 2011 and that of 'one hire for five exits' during 2012–2016.
- Reduction of employees on short-term contracts by 30 per cent in 2010, 50 per cent in 2011 and 10 per cent annually during 2012–2016.
- Mergers of municipalities and reduction of their number by two-thirds and of local government personnel by 50 per cent.
- Labour reserve and mobility schemes through which staff are either reallocated to new posts or dismissed after a certain period on the scheme, during which they receive 75 per cent of their wages.
- Closure, mergers and downsizing of public and private law legal entities (for example, railways, public broadcasting company), which entailed dismissals.

Welfare state retrenchment to reduce social spending

The first EAP and MTF 2012–2015 aimed at reducing expenditure on social transfers from 20.8 per cent of GDP in 2009 to 17.3 per cent in 2015. In 2010, social spending fell by 9.6 per cent due to pension reform and welfare state retrenchment. In line with the Economic Adjustment Programme, a radical pension reform was adopted in summer 2010. This introduced a two-pillar pension system (basic means-tested and contributory pension) to replace the former one-pillar pay-as-you-go system subsidised by the state. The state is now financially responsible only for the basic pension. The reform raised the qualifying period for full pensions to 40 years by 2015 and indexed this period to life expectancy hereafter. A new way of calculating the pension level was introduced, along with heavy penalties for early retirement (6 per cent reduction per year) in order to substantially reduce wage replacement rates. This same pension reform merged all social security funds into three by 2018 and brought the pension system of civil servants into line with the private sector pension system by eliminating all its more favourable provisions. In October 2011, supplementary pensions provided by various pension funds of employees were cut by 15–30 per cent and lump sum pensions for civil servants and some categories of banking and public enterprise employees were also reduced by 15–25 per cent. A new list of hazardous occupations took effect and payment of disability pensions was suspended until all cases are re-examined. In February 2012, main pensions exceeding 1,300 euros were further cut by 12 per cent and supplementary pensions reduced by 15 per cent, on average. At the same time, the supplementary pension system was revamped. All funds were merged into a single one, while the existing defined-benefit pay-as-you-go system was to be gradually replaced by a notional defined-contribution system. Last but not least, in November 2012 the legal retirement age was increased from 65 to 67 years, taking effect on 1 January 2013.

New pension reforms to take place in 2014 are pending

A series of other reforms also aimed at making savings in welfare state expenditure: reduction of ordinary unemployment benefits by 22 per cent and a tightening of criteria for seasonal unemployment benefits; closure of the two public agencies responsible for housing policy and employee recreational programmes (social tourism, free access to cultural events) funded by employer and employee contributions; targeting of social benefits and rationalization of expenditure on social programmes; increased

admission fees and co-payments for outpatient and diagnostic services in public hospitals; exclusion of many drugs and diagnostic tests from the list of those reimbursed by social security; reduction in overtime pay for their doctors; mergers of public hospitals and clinics and closure of public primary health units in urban centres; mergers of public schools and reduction of their number by 14 per cent; drastic cuts in municipal budgets for schools, crèches and nurseries; a 50 per cent reduction in university budgets and one of 40 per cent in those of public hospitals between 2009 and 2013. Increases in school class size, reduction in the number of employees on short-term contracts, non-replacement of those who retire and reductions in overtime payments (especially for medical and nursing personnel in hospitals) are deteriorating the quality of education, health and social care services, thus putting pressure on the family as welfare provider. Positive developments concern the rationalisation of health care expenditure through lower negotiated prices for medicines paid by social security funds and the implementation of an e-prescription system and a central e-procurement system for hospitals.

Last but not least, social security agencies, public hospitals and universities were re-categorised as private investors and their reserves placed in sovereign bonds were reduced by half during the sovereign debt restructuring in spring 2012.

Increasing public revenues from taxes and privatisation

Although tax measures under the EAPs were in principle meant to increase public revenues, in practice they have reduced tax shortfalls caused by recession and falling income. Tax revenues declined by only 10.1 per cent between 2009 and 2013, when GDP contracted by 20.8 per cent and incomes by 35 per cent. This is due mainly to a great increase in the tax burden on those already paying taxes and – to a lesser degree – to the broadening of the tax base. Privatisations have also compensated for the negative income effect on public revenues in recent years. Revenue-increasing measures represent 41.4 per cent of the overall fiscal consolidation effort through 2010–2013 (Anderson 2013).

Tax measures in 2010 focused mainly on indirect taxes: VAT was increased by 20 per cent and excise taxes on fuel, cigarettes and alcohol by 33 per cent; new indirect taxes; extension of VAT obligation to previously exempted economic activities; application of a progressive taxation scale on inheritances and bequests; imposition of ‘crisis levies’ on prof-

itable firms, high value real estate and households with high incomes; increase in taxation on Church real estate and introduction of a tax on Church property income; tax settlement for all uncontrolled, outstanding or litigious cases of firms and the self-employed with tax authorities; and revaluation of fines on unauthorised buildings and settlement of urban planning infringements. Although some of the above measures increased the fairness of the tax system, the rise in the indirect-to-direct tax ratio (from 1.37 in 2009 to 1.63 in 2010) points to an overall regressive impact of the EAP's tax measures on income.

New tax measures were adopted in summer and autumn 2011. They were also clearly regressive and led to enormous social protests against their unfairness and unsustainability for low and medium income and vulnerable social groups. They include the reduction of tax-free personal income thresholds from 12,000 to 5,000 euros; the abolition of tax exemptions for disabled persons, parents of many children and so on; the elimination of tax credits, deductions and invoice based tax refunds; a 60 per cent increase in the criterion for presumptive taxation; the establishment of an extraordinary levy on all real estate, without exceptions, collected through electricity invoices; a reduction in the threshold for the individual property tax and an increase in the minimum tax rate. Also, a permanent solidarity contribution of 1 to 4 per cent, depending on income, was imposed on all physical persons with income above 15,000 euros, and a permanent levy of either 400 or 500 euros on professionals and the self-employed; VAT rates of certain of products and services and other indirect taxes were raised. The unemployment solidarity contribution for private sector employees was raised by 1 percentage point and for civil servants by 2 to 3 percentage points, while a monthly fee was imposed on the self-employed for insurance against unemployment.

In 2013 came comprehensive reforms in income and property taxation. The former was legislated in January 2013 and its main elements were: a reduction of income tax rate bands from eight to three; the elimination of tax credits on mortgage interest payments, life insurance payments, student expenses, tax allowances for children, the tax-free personal income threshold for the self-employed and professionals, the special tax regimes based on imputed income for farmers and seamen; and the restructuring of the tax regime for corporate profits, resulting in a reduction of the gross tax rate on distributed profits from 40 per cent to 33.4 per cent. The above reform reinforced the tax squeeze on lower and middle classes and reduced taxation on corporate profits.

The reform of property taxation was legislated in December 2013. It introduced a new unified property tax unrelated to the level of income, which abolished the tax-free threshold of the previous property tax and did not exclude from taxation property and land that is not being used or exploited. It is thus expected to create social injustices.

From the above presentation it is evident that, despite some rebalancing measures, tax policy since 2010 has not corrected the great fiscal injustices of the past and has even aggravated them. It has imposed a tax squeeze on the lower and middle classes, while high income and property owners have retained their immunity vis-à-vis tax avoidance and evasion. The lack of political will on the part of all Greek governments since 2010 to curb tax evasion through cross-border capital transfers became patent in the case of the 'Lagarde list' scandal. It can be also discerned in the reluctance of tax authorities to control the activities of the numerous off-shore companies at home and the granting of new tax exemptions and favours to maritime capital (Law 4141/2013).

Turning to the proceeds of privatisations, the privatisation programme, which is part of the current (second) Economic Adjustment Programme, encompasses all public firms and agencies (banks, transport companies, ports, airports, utilities, energy, telecoms, gaming industry) and state-owned real estate. Privatisations started with banks and the gaming industry, but they will soon extend to public utilities that are crucial for the provision of basic goods at low prices (electricity, natural gas, water supply). A recent law, passed last summer, has already created a small company endowed with some of the most profitable assets of the public electricity company, to be sold as soon as possible. Besides, many laws have loosened environmental protection and lately restricted free access of citizens to coasts to enable the sale of public real estate.

4.3 Dismantling the employment model and undermining trade unions and collective bargaining

The two EAPs included a large number of labour market and product market reforms that dismantle the Greek employment model and undermine trade unions and collective bargaining. These reforms serve several goals at once: reduction of public sector wage bill and radical downsizing of this sector; opening up opportunities for capital concentration in services through a substantial decrease in self-employment; and internal

devaluation by drastically reducing nominal wages and attacking employee rights in the private and public sectors.

Drastic reduction in public sector employment and self-employment

Retrenchment in public sector employment is the outcome of a combination of direct measures (parsimonious hiring, labour reserve, dismissals) and indirect ones (closure, restructuring and privatisation of public entities and companies). In 2010, public sector employment decreased by 10 per cent, while the Greek government committed itself to reduce public employment by 150,000 over 2011–2015, including 15,000 dismissals in 2013–2014. Official administrative records indicate that employment in general government declined by 34 per cent between the end of 2009 and the end of 2013. Further declines are expected in 2014 and 2015, not only in general government but also in public agencies/companies before or after their closure or privatisation.

As for self-employment, a number of converging factors are curtailing it. First, recession is putting great pressure on own-account workers and micro-entrepreneurs, leading to mass closures of micro-businesses. Secondly, the government has removed restrictions on competition, business and trade in more than one hundred regulated professions. This has intensified competition and reduced minimum compensation/returns in a period of drastically falling demand, pushing great numbers of the self-employed out of business and inducing a concentration of capital in the corresponding activities. Between 2008 and 2011 the number of firms with up to nine employees decreased by 15.2 per cent (SBA Fact Sheet).

Massive attack on employees' rights

The following measures have been adopted: reduction in the notice period for individual dismissals from a maximum of 24 to a maximum of 4 months and in the level of severance pay from 2–24 months to 1–6 months (with prior notice) and 2–12 months (without prior notice); increase in the minimum threshold for collective dismissals from 2–3 per cent to 10 per cent; abolition of clauses on tenure applying to all public sector employees who are not civil servants and transformation of their labour contracts into open-ended ones; labour reserve/mobility schemes and dismissals in the public sector; extension of the probation period for new hires from two months to one year; extension of the cumulative maximum duration of fixed-term contracts from two to three years

and easing the conditions for derogations; extension of maximum duration of spells of employment for temporary agency workers from 18 to 36 months; extension of maximum duration of rotating work at a given firm in case of financial difficulties from six to nine months per year – it can be now unilaterally applied by the employer after consultation; the employer can now decide unilaterally on layoffs of up to three months in firms with up to 5,000 employees; part-time work is now allowed in public utilities; the employer is now allowed to transform the labour contract from full to part time with only the consent of the employee; abolition of the 7.5 per cent wage premium for short part-time working and of the 10 per cent premium for each working hour of part-timers over the agreed daily time; reduction of overtime pay by 20 per cent; increase in weekly working time in the public administration from 37.5 to 40 hours; easing of flexible working time arrangements.

The most important of the above measures are those making individual and collective dismissals easier in the private sector, abolishing tenure for the employees of public enterprises and introducing the labour reserve/mobility schemes and dismissals in the public sector. They entail the dismantling of a core feature of the Greek employment model, namely strong employment protection of permanent employees.

Defeating the unions, undoing collective bargaining, expanding individual bargaining

Internal devaluation, the second of the key objectives of the EAPs, required substantial reductions in nominal wages and labour costs, resulting in lower prices. Judging labour cost decreases of about 5 per cent in 2010–2011 unsatisfactory, the authors of the second EAP introduced a quantified target (15 per cent) for labour cost reduction in the business sector of the economy in the three-year period 2012–2014.

The required overall adjustment in labour costs (–20 per cent) necessitated the dismantling of the wage-setting system by undoing collective bargaining, defeating the unions and promoting individual bargaining in the private sector. In the new context the national minimum wage could play the role of a safety net. The dismantling of the wage-setting system was achieved with the following set of measures:

- Collective bargaining on wages was suspended in all public utilities, agencies and undertakings, where cuts in nominal wages

were introduced by law in 2010 and 2011. In 2012 a law imposed the civil servants' wage grid on the employees of all private law legal entities that belong or are subsidised by central and local government. Collective bargaining on wages has thus been practically curtailed in this fundamental pillar of the pre-crisis wage-setting system where union power has been concentrated for decades.

- Decentralisation of collective bargaining at the firm level. In the case of overlapping issues and clauses, company-level collective agreements take precedence over sectoral and occupational agreements, even if their provisions are less favourable for employees. Company-level agreements can now be signed not only by unions but also by associations representing at least three-fifths of a firm's staff, who can easily be subjected to employer manipulation in small firms.
- Suspension for 2012–2013 of the extension of the coverage of sectoral and occupational collective agreements to non-union members by the Minister of Labour. This induces firms to quit employers' organisations, thus indirectly undermining collective bargaining at the sectoral or occupational level and promoting individual bargaining between employers and employees on wages.
- Collective agreements which expire now remain in force for a maximum of three months (previously six months). If a new agreement is not reached during this period, a number of allowances are no longer applicable after its expiration and until a new collective agreement is concluded or a new individual contract is signed.
- Arbitration now takes place only when agreed by both employees and employers. Before the reform, unions could have recourse unilaterally, provided that employers had rejected the outcome of mediation. Moreover, arbitration now applies only to the base wage and not to other remuneration. Trade union power against intransigent employers during negotiations has thus been weakened.
- In February 2012, an Act of Cabinet established wage floors below the national minimum wage set by the National General Collective Agreement (NGCA); the wage floor for those aged 25 years and over was set at 586 euros, which is 22 per cent lower than the national minimum wage of the NGCA, while the wage floor for young people below 25 years of age and apprentices 15 to 18 years of age was, for the first time, differentiated from that for older workers and set at 511 euros, that is, 32 per cent lower than

- the national minimum wage of the NGCA. By the same Act, all statutory and collective agreement clauses that provide for automatic wage increases, including those based on seniority, were suspended until the unemployment rate reaches 10 per cent.
- In November 2012, a law introduced a new way for setting the minimum wage rate. This will be legislated by the government after consultation with social partners and experts. The longstanding tradition – since 1936 – of establishing wage floors through national-level collective bargaining was thus abolished.

Apart from the above path-breaking institutional changes, the big rise in dismissals and unemployment undermines collective bargaining and union power even more. All collective agreements at all levels concluded in recent years provide for wage freezes or – more frequently – for wage reductions, while many employees have accepted or have had imposed on them wage reductions at the company level ranging from 10 to 40 per cent.

Last but not least, new measures were recently announced for autumn 2014 under MoU2, which represent a further attack on union power. These include restricting the right to strike and the freedoms of union representatives, allowing lock-outs – which are currently illegal – and changing the financing of unions in order to reduce their financial resources. The above measures point to the ultimate goal of the Economic Adjustment Programme – and of the social and political forces that support it – namely to get rid of unions altogether.

5. Killing the 'patient': the dramatic consequences and impasse of austerity policy

The neoliberal offensive has severely disrupted social cohesion, not to mention people's lives and morale, especially the most vulnerable, and it is leading the economy to collapse. Four and a half years of imposed economic 'adjustment' have shrunk Greece's GDP by 20.8 per cent and led to huge wage and pension cuts, excessive taxation of low and medium incomes and a retrenchment of the welfare state. Unemployment climbed from 9.5 per cent in 2009 to 27.3 in 2013. Female and youth unemployment currently stand at 31.1 and 53.1 per cent, respectively (May 2014), while families are experiencing major income losses and are increasingly unable to provide for their offspring. Real wages per head in the whole economy fell by 25.6 per cent between 2009 and 2013, while about one-

third of private sector employees sometimes have to wait several months for wage arrears to be paid. At the same time, social protection is being weakened and the quality of social goods and services eroded. Official statistics indicate that the population living in poverty and social exclusion climbed from 27.6 per cent in 2009 to 34.7 per cent in 2012. Furthermore, a large number of people and households cannot afford food, electricity, heating and shelter, while one-third of the population no longer has health insurance and thus has access only to the emergency rooms of health centres and public hospitals in the National Health System.

Table 2 Main economic indicators, Greece, 2009–2013

	2009	2010	2011	2012	2013
Real GDP	–3.1	–4.9	–7.1	–7.0	–3.9
Private consumption	–1.6	–6.2	–7.7	–9.3	–6.0
Public consumption	4.9	–8.7	–5.2	–6.9	–4.1
Investment (GFCF)	–13.7	–15.0	–19.6	–19.2	–12.8
Exports of goods and services (volume)	–19.4	5.2	0.3	–1.7	1.8
Imports of goods and services (volume)	–20.2	–6.2	–7.3	–13.8	–5.3
Current account balance (% GDP)	–14.4	–12.8	–11.7	–4.6	–2.4
Employment	–1.1	–2.3	–6.1	–8.7	–4.1
Unemployment rate (% labour force)	9.5	12.6	17.7	24.3	27.3
Inflation (harmonised CPI)	1.3	4.7	3.1	1.0	–0.9
Real wages per head	2.8	–6.3	–6.5	–4.6	–5.2
Unit labour costs	6.2	–0.1	–1.8	–5.1	–6.8
Industrial production	–9.4	–5.9	–7.8	–3.4	–3.6
Retail – turnover at constant prices	–9.3	–6.9	–8.7	–11.8	–8.4
Construction (volume)	–17.5	–29.2	–28.1	–26.1	–25.7
Travel receipts at constant prices	–11.4	–12.2	6.4	–5.9	17.9
Receipts from sea transport	–29.4	13.8	–8.6	–5.7	–9.0

Source: European Commission (2014), Bank of Greece (2014).

From an economic perspective, the Economic Adjustment Programmes instigated a spiral of austerity–recession–austerity. The deleterious impact of this kind of economic adjustment was recently recognised by the OECD in its latest economic survey on Greece:

Apart from being larger than initially envisaged, this consolidation has had a larger impact on activity than had initially been estimated even though other factors, most notably the surge in political uncertainty and fears of an exit from the euro area also contributed to the lower-than-previously-forecast growth. Until the end of 2012, tax revenues have fallen persistently below expectations and reforms have proven difficult to implement, resulting in major slippage in areas such as health. This has required greater spending cuts to meet targets, depressing domestic demand. The general government had also built up sizable payments and to a lesser extent tax-refund arrears, which stood at 4.6% of GDP at end-2012. This reduced private sector liquidity in a context of very tight credit conditions. (OECD 2013: 17)

Moreover, the sizeable reduction in unit labour costs has not had any significant impact either on prices or on exports (Table 2). In 2010 inflation rose while in 2011 it remained high because hikes in VAT and other indirect taxes more than compensated for the income-effect of austerity on prices. In 2013 Greece experienced deflation of 0.9 per cent, but the harsh cumulative reduction in nominal wages through 2009–2013 was clearly not followed by a similar fall in prices, thus invalidating ‘internal devaluation’ as the mechanism par excellence for wiping out the current account deficit. As for Greece’s export performance in recent years, this seems to have varied with demand conditions in international markets, not with changes in unit labour costs at home. It is also noteworthy that, although the current account deficit has shrunk considerably since 2010, this is predominantly accounted for by the plummeting of imports caused by the great fall in incomes. This means that the small deficit – 2.4 per cent of GDP in 2013 – that was achieved after six years of recession is unsustainable. It will start to increase as soon as recovery appears and the economy starts growing again. Even more worrisome is that it may expand very rapidly due to Greece’s weakened productive base.

Deepened and permanently fuelled by persistent fiscal consolidation, the recession is still destroying thousands of jobs, own-account workers and small and medium-sized businesses and seriously eroding the tax base and social security finances. Since 2010 very large and continuous-

ly growing parts of the Greek population have perceived and protested against the disastrous nature and socially unfair character of this kind of ‘economic adjustment’. Social protest has focused on the overthrow of the MoU, rejection of the various packages of measures and refusal to repay the debt. People in the streets and squares, in private and public meetings and conversations blame the Troika – and also the German government – that has imposed such policies on the Greek people, as well as the country’s political and economic elites who have ruined their lives and the future of their children, while still enjoying their own privileges and transferring their wealth abroad.

Last but not least, the six consecutive years of recession have so far annulled the gains from sovereign debt restructuring and bank recapitalisation. They have not only put the economy into a debt trap that perpetuates the unsustainability of the sovereign debt – forecast at 177.2 per cent of GDP for the end of 2014 – but have also transformed the low indebtedness of households at the start of the crisis (43 per cent of GDP) into over-indebtedness, which represents a timebomb in the foundations of the banks recently recapitalised with the monies of external loans and at the expense of taxpayers. In March 2013, 27.5 per cent of mortgage loans and 42.5 per cent of all consumption loans were non-performing. A law passed in December 2013 removing protection from foreclosures – except for the first habitation, up to a certain threshold – is expected to deprive thousands of middle-class families of their real estate.

6. What prospects – what alternatives?

The Greek experiment has proved the patent failure of the three basic tenets of economic orthodoxy in Europe and elsewhere. The first tenet maintains that austerity is expansionary and represents a way out of the crisis; the second that sovereign debt can be repaid by primary budget surpluses; and the third that lowering labour costs leads to falling prices and export-led growth. Austerity has instead led to a Troika/state-induced depression; sovereign debt is unsustainable and needs restructuring; and lower labour costs are unable to stimulate exports.

Despite the manifest failure, the leading powers in the euro zone and the ECB are unwilling to abandon the recipe. The new German government has ruled out a new ‘haircut’ on Greek sovereign debt held by the official sector, while alternative, less radical forms of sovereign debt restructur-

ing, accompanied by a new loan, are being considered instead. If this finally occurs, the new loan agreement will be tied to a third Economic Adjustment Programme and new economic policy conditionality aimed at ensuring that the neoliberal 'structural adjustment' project that commenced in 2010 is completed. The two main issues of the next two years are privatisations and foreclosures of private real estate. The privatisations of public companies, agencies and real estate are of great interest for foreign multinationals, while foreclosures of private real estate for outstanding debt to Greek banks are the precondition for a collapse in real estate prices and an ensuing buying-up of land and houses/buildings by big real-estate companies at fire-sale prices. At the same time, tight fiscal policy will continue in order to accumulate sizeable primary surpluses that will be used to repay sovereign debt, not to stimulate real economic growth and job creation. However, recession, stagnation and even low economic growth heighten the debt-to-GDP ratio and exclude the possibility of repaying the total amount of debt in the future.

Much more important, however, is that depression-level unemployment – 72 per cent of which is already long-term – will further erode social cohesion and fuel emigration among young educated people, thus depriving Greece of valuable human resources that might enable it to establish a new growth pattern based on technological upgrading and innovation. At the same time, the all-encompassing privatisation programme will further destroy important engines of endogenous growth by permanently depriving the state of strategic industrial-policy tools that could be used to influence the pattern of growth. According to the economic rationale of the Economic Adjustment Programmes, growth should depend predominantly on investments by foreign multinational capital and the most internationalized segments of Greek capital. A host of structural economic policy measures in the Economic Adjustment Programmes, besides the huge privatisation programme, are destined to offer incentives to such major investors. The greatest incentive will be an impoverished working class deprived of its rights and a vast labour reserve army created by mass unemployment.

Against the continuation of this socially regressive recipe, progressive political forces in Greece are proposing a growth strategy which allows for fiscal adjustment through an increase in taxable income and radical tax reform and makes use of primary fiscal surpluses and external financing (from the EU and other sources) for poverty alleviation and public investment. The preconditions for this alternative strategy are:

the end of recessionary policies; a moratorium on servicing sovereign debt and a write-off of a substantial part of the remainder and a growth clause for repayment of the rest; and a 'Marshall Plan for Europe' which would benefit in particular – though not only – EU countries and regions that have suffered most from crisis and austerity.

Such an alternative can be negotiated only at the EU level and is directly associated with the debates on the EU's exit strategy from the crisis, as well as the future of EMU and the European integration project. Some of the fundamental questions in this debate are as follows. Is coordinated austerity and the promotion of export-led growth in all member states a viable exit strategy for the EU as a whole, or, alternatively, would coordinated wage-led growth driven by the expansion of the Single Market be a more economically and socially sustainable strategy? Can the European Social Model survive in the European North if workers and people in the European South are deprived of their social rights and their countries forced to build their new competitive advantage on social dumping? Can the EMU survive in the face of growing economic and social divergence among member states? What are the political/ institutional prerequisites of a more solidaristic and cohesive EMU and EU?

In a European perspective, Greece was the first euro-zone country to fall victim to the global rise in sovereign debt after the first phase of the global financial crisis. It was also the first to switch to a full-fledged neoliberal economic adjustment process as a way out of the crisis. The new Treaty on Stability, Coordination and Governance and the Euro Plus Pact are proposing the same way forward for all EU countries; that is, to tighten fiscal policy and stimulate export-driven growth through competition on labour costs, taxes and welfare state retrenchment. However, coordinated restrictive fiscal policies are a self-defeating strategy for growth in the EU. It does not only make the economic adjustment of the European periphery extremely difficult but is also clearly menacing the whole continent with deflation and secular stagnation.

Given the generalised trend towards deflation, stagnation and socially regressive policies and the threat of EMU disintegration, it has become evident that there is a need for new hegemonic socio-political blocs at the national level and a decisive shift in the balance of political forces, along with coordinated action at the European level, if alternatives to the current neoliberal project for Europe are to become credible. The Greek people would be the first, but not the only beneficiaries.

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Irish paradoxes: the bursting of the bubbles and the curious survival of social cohesion

James Wickham

1. Introduction

Until 2008 Ireland was the neoliberal poster boy. With its economic growth at times reaching Asian proportions for over two decades, the so-called ‘Celtic Tiger’ apparently demonstrated the validity of liberal economic principles: global openness, low taxation and a flexible labour market. Ireland was held up as a model by the (then) UK Shadow Chancellor George Osborne as a lesson for the United Kingdom and by the President of the European Commission, Manuel Barroso, as a model for Europe.

This chapter begins with a description of the *bubble labour market* of the final years of the Celtic Tiger economy and its sudden collapse. The second part of the chapter shows how the road to the crisis was prepared by four core features of the Irish model: the veto-power of foreign direct investment (FDI), the financialisation of everyday life, the importance of the banking sector and, last but not least, social partnership. The crisis has entailed unemployment, falling living standards, weaker employment protection, mass emigration and unsustainable personal debt. Nevertheless, the core institutions of the Irish social settlement have proved remarkably durable – enough to ensure that the economic crisis has not generated a complete political crisis.

2. The bubble labour market

Conventional accounts of recent Irish political economy contrast a ‘good boom’ with a subsequent ‘bad bubble’. The boom was characterised by export-led FDI lasting from the late 1980s through to the start of the twenty-first century, after which it was overlaid with a domestic asset-

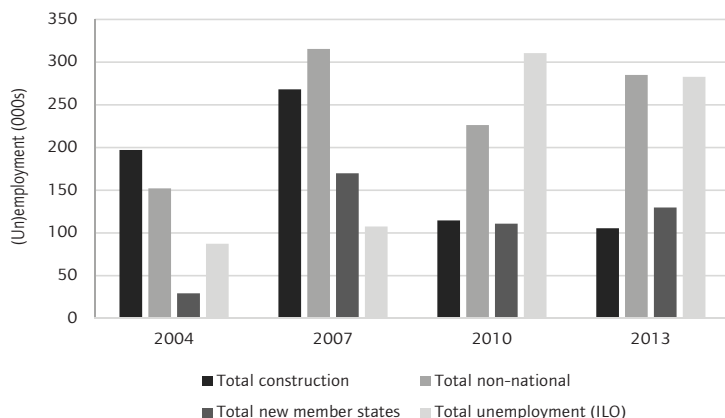
based bubble. After the slump of the early 1980s, Irish economic growth began again in the late 1980s, with GDP growing both absolutely and in per capita terms through the 1990s, reaching 10.7 per cent in 2000. GDP growth continued for the first few years thereafter, reaching 6.0 per cent in 2007. This time however, the driving force was the expansion of domestic credit leading to rapidly rising asset prices: a classic property bubble. The collapse came in 2008, when GDP contracted by 3.0 per cent and as much as 7.1 per cent in 2009 (European Commission 2010).

These developments were reflected in the labour market. In the mid-1980s Ireland had mass unemployment and mass emigration. In 1985, for example, unemployment stood at 16.8 per cent (in the then EU only Spain was higher, at 21.6 per cent). As GDP growth began, recovery in the labour market was initially slow. As late as 1996 the unemployment rate was still 9.9 per cent, although it fell to 5.7 per cent in 1999. The number in work was growing, but so too was the labour force: Ireland's late baby boomers of the 1970s were entering the job market, more women were now looking for work and emigrants were returning. After 2000 employment continued to grow, reaching a peak of 2.1 million in 2007, an increase of more than 50 per cent on the 1997 figure (European Commission 2010).

From about 2000 employment growth was driven largely by immigration. Between 2001 and 2007 the number of Irish people in work rose from 1.55 million to 1.66 million, an increase of just over 100,000. By contrast, in the same period the number of foreigners – 'non-nationals' in official parlance – in work rose from 77,000 to as many as 312,000, an increase of nearly a quarter of a million! By the time of the 2006 census Poles had become the second largest group of non-national citizens in Ireland after the British, and by 2008 estimates of the total Polish population were as high as a quarter of a million. There was more Polish than Irish spoken on the streets of Dublin. This immigration was a mass labour migration within the European Union: new member state (NMS) migrants had the same employment rights and largely the same social welfare rights as Irish citizens: unlike illegals, they could not be threatened with deportation, unlike immigrants on work permits they were not tied to specific employers.

Total employment in construction rose to a peak of 269,900 in 2007, at which point it comprised 13.4 per cent of total employment. Within the EU only Spain had a similar proportion (CSO 2008: 18). As Figure 1

Figure 1 Total employment and unemployment 2004–2013



Source: Derived from CSO (2014).

shows, in just three years between 2004 and 2007 the number in work in construction rose by over a quarter. At the end of 2007, 18.3 per cent of all construction jobs were held by immigrants (13.5 per cent from new member states) and there was some truth in the popular conception of the Irish building industry in terms of Polish immigrants building apartment blocks for the next wave of new arrivals to inhabit. However, unlike in Spain, immigrants spread through most of the occupational structure. At the peak of employment in 2007 immigrants from the new member states accounted for 8.1 per cent of all persons in work, including 20.2 per cent of all jobs in accommodation and food; 11.5 per cent of all jobs in manufacturing but also 13.9 per cent of jobs in administration and even 2.6 per cent of jobs in financial services. Indeed, despite an over-representation in less skilled jobs, 7 per cent of all NMS immigrants in work were employed in professional and managerial occupations (CSO 2011a).

The astonishing employment growth shows how, just as Ireland had an asset bubble, it also had a labour market bubble. There are striking historical parallels with the booms in areas of the settler societies of the nineteenth century, such as Australia and the United States: extraordinarily rapid growth in which populations could double in ten years;

'boosterism', propaganda that involved a suspension of normal beliefs so that continued exponential growth seemed possible; and, finally, dramatic crashes when growth ceased and population fell (Belich 2010; Reeves *et al.* 2010). Just as in the settler booms the rapid growth of employment depended on the continued inflow of new settlers, so in a bubble labour market there is a continued inflow of new workers. The notion of a territorially bounded labour market collapses.

The apparently inexhaustible supply of labour involves a paradox. On one hand, migrants flood in because they assume they will obtain well-paid jobs. On the other hand this continued inflow reduces wage inflation: demand for labour rises, but so does supply. The paradox can be resolved when we realise that there are two frames of reference involved. For the migrant the point of comparison is the wages 'back home' (Waldinger and Lichter 2003); for the employer the comparison is wages in the local labour market.

Bubble labour markets are flexible labour markets. Rather unusually, this flexibility suits both sides of the employment relationship. In the bubble, employers need labour and are prepared to take on almost anyone. New immigrants present the problem that the qualifications on offer no longer fit into the well-established categories with which employers are familiar, while employers lack the time or expertise to verify qualifications. At the same time, because there appears to be an inexhaustible supply of suitable people, employers face little pressure to develop labour-saving innovation or alternative employment strategies.

3. Creating the bubble

This bubble was generated by four key features of the Irish socio-economic model that became more pronounced as the boom of the 1990s turned into the bubble of the mid-2000s.

First, the central role of FDI in the national growth strategy provided the overall framework for the crash. From the 1930s to the 1950s the newly independent state had pursued a policy of economic protectionism. Partly for this reason, Ireland did not share in Europe's post-war reconstruction. In 1957, however, the country began to abolish import duties, create tax benefits for exporters and aggressively pursue foreign direct investment producing for export to the developing European mar-

ket.¹ Starting initially in relatively simple assembly type manufacturing jobs, FDI has increasingly focused on high technology manufacturing (electronics, medical instrumentation, pharmaceuticals), software and financial services. In the early years foreign-owned firms came from elsewhere in Europe, including some German firms looking for a low-cost manufacturing base; slightly later these were joined by Japanese firms seeking access to the European market. Already by the 1980s the state agency responsible for FDI, the (then) Industrial Development Authority, had a reputation internationally as one of the most effective organisations in this area and had begun to successfully target specific sectors of potentially mobile investment, especially electronics and pharmaceuticals. Since then there have been several waves of FDI in 'high tech' sectors, and despite its size Ireland has long had one of the largest volumes of FDI within the EU (Barry 2007).

Far more was involved than manufacturing. This investment was increasingly American. As of 2008, US affiliates directly employed 91,000 in Ireland, representing about 5 per cent of all employment in the country (Irish Times 2011b). All of this occurred against a background of the changed role of Irish politics in the United States. Irish-Americans long ago broke out of the ethnic ghetto and their entry into the US corporate elite has become an important resource for Irish economic policy. Indeed, the attraction of US investment to Ireland has become one of the most successful examples of elite diaspora politics globally.

The policy rhetoric surrounding FDI has often insisted that foreign firms will generate domestic spin-offs, so that FDI will become the motor of a more broadly based economic development. The reality is rather more complex. Especially in software, but also in medical instrumentation, a parallel indigenous industry has grown up (O Riain 2004; Giblin 2011). These Irish firms are not necessarily direct suppliers to the foreign sector even though they share a professional and managerial labour market. These firms are also very different from traditional domestic industry, because many serve the international market from the outset. The combination of cheap air travel and electronic communications means that they are 'born global' (Wickham and Vecchi 2008).

1. There had been foreign (almost entirely British) ownership of manufacturing industry in the protectionist period, but this was in the very limited industry servicing the small domestic market and the extent of such ownership was legally restricted.

The reliance on export-oriented FDI has been a leitmotif of Irish economic policy for over half a century. It rests on an almost complete national consensus and has never been seriously challenged, even by the marginal socialist and left nationalist groups. Initially the key policy instrument was various forms of state grant to foreign companies, but these have been increasingly replaced by tax relief and then simply by the low corporate tax rate. Of course, firms' location decisions involve far more than this: English language, political stability, access to the European market, wage levels and competitiveness all play a role. At times rather grandiose claims have been made for the virtues of Irish education and, more recently, for the strength of relevant scientific research in Irish universities. Nonetheless, state policy towards FDI has paid decreasing attention to social and physical infrastructure and has focused increasingly on the low corporate tax as the key incentive for FDI. This ensured that a political conflict with other EU member states was inevitable. Such conflict was further promoted by the Americanisation of Irish public discourse and economic thought, the promotion of 'Boston not Berlin' as a social model, and the direct and indirect influence of the Dublin American Chamber of Commerce on political decision-making.

A second key precondition for the bubble was the steadily increasing financialisation of everyday life (Froud *et al.* 2007). Central here was the new role of housing. Ireland has long had a high level of owner-occupation and this was accentuated by the policy of selling 'council housing' (social housing) to tenants from the 1980s. Before the start of the bubble 82 per cent of all households were owner-occupiers, one of the highest levels in Europe, but until 2000 about 50 per cent were debt free (Fahey 2003). This historic extensive personal home ownership was then transformed by the development of retail financial services and extensive mortgage credit, creating a particular variety of 'residential capitalism' (Schwartz and Seabrooke 2008). In this new model the home loses some of its distinctive emotional features and becomes in part just another type of property. The different types of private property become less distinct because they become *fungible*: because they can be easily bought and sold their owners can change the form in which their wealth is held. The development of financial services allows home-owners to use their property as security for further borrowing. Privately owned housing can be used as security for borrowing for consumption ('the house as ATM') or for purchasing further assets.

The transformation of the pension system also expanded private asset ownership. Across the private sector (and in state enterprises) defined benefit schemes were increasingly replaced by defined contribution schemes, so that individuals ended up owning various financial assets from which (hopefully) they would receive their pension. The privatisation of the national telephone company was explicitly designed to further such ‘people’s capitalism’, but unlike in the United Kingdom in the 1980s there has been no further mass privatisation of state property (Sweeney 2004).

This financialisation has two immediate consequences. For an increasing number of people, life chances are no longer determined purely by their occupation but also by their property and how they manage it. This can create new economic success but, as the Irish soon discovered, it also brings new and bigger risks.² Secondly, public services have to be purchased. De-commodification as described by, for example, Esping-Anderson (1990) is going by the wall and welfare is being re-commodified. During the boom Irish households bought private health insurance in order to access privately provided health care (Burke 2009) and an increasing proportion abandoned the public sector for the private schooling of their children. Often described as late or incomplete, the Irish welfare state became a ‘residual welfare state’ closer to Boston than Berlin.

This financialisation inevitably meant that the boom would become a bubble. It made property ownership into an obsession of large swathes of Irish society, paradoxically creating a new rental market as larger numbers of people invested (borrowed) money in ‘buy to let’ property. Much of this property was overseas: according to one estimate, by the peak of the bubble an estimated one in ten of the Irish population owned property abroad (Guardian UK, 3 April 2011; Wickham 2006). In this respect, Ireland was following the United Kingdom, as described by a manager of one of the largest UK estate agents:

We are the first in Europe to see property as an asset class. We use it as a substitute for pensions and now are buying overseas. (Fay Davies, Director of International Property at Jackson Stops & Staff, Financial Times, 29.10.2003)

2. Back in the 1980s sociologists discovered the new ‘risk society’ (Beck, 1986); very few noticed the return of the traditional risks of the market.

Unfortunately such purchasers ignored the legal health warning: ‘the value of assets can go down as well as up’ ...

In the United States the expansion of consumer credit occurred when real wages were stagnant; credit functioned temporarily to provide illusory growth. In Ireland the credit expansion occurred when real wages were actually rising. Cheap credit did not compensate for zero growth, as in the United States, but instead accelerated the rising consumer expenditure which wages and salaries were already financing. Furthermore, both lenders and borrowers assumed that incomes would continue to rise; any pause in continuing economic growth would make the system unsustainable.

A third cause of the bubble was the nature of the banking system. Conventional economic commentary focuses on the combination of euro-zone membership (cheap credit) and weak banking regulation. However, this ignores how the fundamental political commitment to an ‘Anglo-Saxon’ financial system in a liberal market economy stacked the cards against any effective banking regulation. Banks have always had a disproportionate role in the Irish economy. During the 1990s the two long-established Irish banks (Allied Irish Bank [AIB] and the Bank of Ireland), like many other banks elsewhere in Europe, were transformed from traditional retail banks into financial services companies, with increasingly competitive marketing of their financial products (Regini *et al.* 1999). Both AIB and Bank of Ireland expanded overseas, purchasing affiliates in the United States and the United Kingdom.

After the crisis of the 1980s, a key element of the national growth strategy became the promotion of the Dublin International Financial Services Centre as a location for mobile global financial services. While Ireland’s low tax rate was certainly an important attraction, today it is conveniently forgotten that ‘light touch regulation’ was explicitly advertised as a reason for financial services companies to re-locate to Ireland. This, too, made tighter regulation of the existing banks unlikely. In this context one small bank (Anglo-Irish Bank) and one building society (Irish Nationwide) could become ‘rogue’ institutions, aggressively expanding their loan books without any regard whatsoever for normal lending criteria. This in turn pushed the traditional institutions down the same road.

The expansion of bank lending had little to do with the foreign-owned sector and was of little relevance to indigenous enterprise; the banks’

major loans were to property developers and to private consumers. The Irish property bubble was based on an extraordinary expansion of credit. In 2002 total mortgage debt was 47.2 billion euros; at the end of 2008 it had more than trebled to 139.8 billion euros (CSO 2008: 8). This enabled large-scale building of houses and apartments, hotels and offices, many of which now stand empty. Until the building boom ended, public finances were in surplus. With entry to the euro zone, Irish banks suddenly had access to cheap credit, which they used for increasingly irresponsible domestic loans. When the boom collapsed, many of these loans became worthless. The cause of the current crisis is that the Irish state took responsibility not just for deposits in Irish banks, but for the banks' entire loan books. The crisis is a crisis of private debt which then became a public one. Trained to worry about state debt, nearly all Irish economists were blithely unconcerned about the expansion of private credit that led to the bubble.

Ireland's dominant political party, the populist Fianna Fáil, has always had close links with the building industry. Now the builders became the core of a new *indigenous* business elite, whose 'buccaneering' business antics³ drove the bubble forward and whose extravagant lifestyles appeared to exemplify the new Ireland.

Paradoxically, a fourth precondition for the bubble was a key feature of the employment system itself: social partnership. Beginning with the *Programme for National Recovery* in 1986, a series of tripartite agreements agreed wage rates across the entire economy. Over time the agreements covered a wider range of policy issues and included other interest groups, especially the so-called 'community sector'. This was partly stimulated by the developing European Union governance system, but also had distinctively Irish sources and features. Partnership spread to areas beyond the workplace, with 'partnership' at local community level hailed by enthusiasts as exemplifying deliberative democracy and social innovation (Sabel 1996). In parallel there was an attempt to develop workplace or enterprise partnership: across the state sector and in a few private companies partnership committees were created which were intended to deliver mutual gains through increased productivity and better working practices (Roche and Geary 2000).

3. Famously, Irish developers took great pleasure in buying landmark properties in London and were rumoured to have purchased the island of 'Britain' in Dubai's new artificial archipelago.

It is of course difficult to judge what would have happened to wages without these agreements, but national agreements probably reduced overt industrial conflict and marginally restrained wages in the private sector, while public sector wages and salaries probably increased more than they would have otherwise. The very rich undoubtedly benefitted most from the boom and above all from the bubble, but overall income inequalities in the mass of the population seem to have remained relatively constant even as incomes rose. Ireland was one of the more unequal societies of the EU15 before the boom; economic growth made everyone better off but did not seriously change relative disparities (Nolan and Maître 2007:41). For everyone in work real wages increased. Those who could not work – or who did not want to work – also gained. Benefit levels were high by European standards (and significantly higher than in the United Kingdom); access conditions were eased; labour market activation was almost non-existent (Grubb *et al.* 2009). What mattered was cash, not public services or social infrastructure. Thus for both employers and unions reducing direct taxation was a priority, whereas improving state services was not. While union activists might bewail the ‘incorporation’ of union leadership, and these same union leaders might welcome the chance to participate, however marginally, in national policy-making, social partnership had popular support because it apparently delivered more jobs and more money (Teague and Donaghey 2009).

Involvement in national agreements ensured that Irish trade unions were not marginalised from decision-making, as happened in Britain. While liberal commentators complained about union power, what is striking is how little partnership achieved. Most dramatically, unions were unable to achieve any right to union recognition, even though at the end of the period they were able to force the creation of the National Employment Rights Agency. Significantly, the remit of this organisation was simply to enforce existing employment legislation! Even when government funds were available, there was no shift towards labour market activation for those who remained outside the labour market. This could have been politically problematic because it would have meant challenging the dependency culture that had become widespread in deprived areas. Less explicable is the failure to tackle deficits in the education system at vocational, secondary and especially primary levels, or to seriously increase Ireland’s notoriously low level of childcare provision. Health expenditure certainly increased, but in the context of growing privatisation and the consolidation of a dual public/private system. In policy areas further removed from traditional union concerns the record was

even worse. In public transport, the unions merely protected their members' short-term interests (Wickham and Latniak 2010), while tolerating a massive expansion of private transport. Significantly, the peak of social partnership occurred at the same time as the complete collapse of spatial planning. Indeed, it is arguable that if Ireland had had effective spatial planning, the building boom would have been restrained.

Gross union membership increased, and unions made determined attempts to recruit new members from the new immigrant workforce in sectors such as construction and hotels and catering, but union membership in no way kept pace with the growth in employment. Furthermore, the crisis of the 1980s had cut a swathe through existing manufacturing employment, thus destroying one of the unions' main heartlands. Whereas new foreign-owned companies in manufacturing in the 1970s had accepted – albeit often unwillingly – trade union membership among their employees, by the 1990s their successors were openly pursuing a non-union policy which national social partnership was powerless to prevent.

An unanticipated consequence of the boom was therefore an ever greater relative concentration of union membership within the state sector. This in turn ensured that union members became disproportionately female and in intermediate occupations. One aspect of the boom has been the undoubted greater efficacy of *sections* of the state administration. However, this change has been much weaker in those state services, especially education and health care, where large numbers are employed. Consequently, Irish trade unions were increasingly perceived as a producers' lobby group, concerned simply to maintain their existing pay and conditions and unwilling to generate the political vision to campaign for improved services. To the extent that social partnership did not involve any substantial 'social wage', it ensured that rising wages were used to buy goods and services on the market, and was complicit in the financialisation process.⁴ Unwilling or unable to challenge the veto power of FDI, social partnership consolidated the overall framework of Irish social and economic development.

4. Given that the relationship between union membership and income is now probably U-shaped (low at the top and bottom of the income distribution).

4. Employment model in the crisis

These features of the national model also helped to shape the particular form of the crisis. Employment in construction has been decimated, while American FDI has become more important than ever. Trade union membership has continued to fall and social partnership has been weakened. Nonetheless, despite rising poverty the core elements of the welfare state have remained and this has prevented any dramatic growth in inequality. A novel feature of the crisis is the indebtedness of a large proportion of ordinary people; immigration has not ended but emigration has reached new heights.

With the end of the speculative building boom, employment in construction was decimated (Krings *et al.* 2011), falling to less than half of the 2007 peak by 2013 (see Figure 1). With the collapse of domestic demand, employment also fell sharply in hospitality and catering, where many immigrants from the new member states had been employed. By contrast, employment in the export-oriented FDI sector has held up well, with job losses compensated for by the arrival of new firms. High tech manufacturing was central to the last wave of FDI, but some of this has now relocated to lower wage parts of Europe. Thus computer firm Dell closed its Limerick plant and moved production to Poland in 2009, but nonetheless in 2011 the company employed 2,200 in Ireland in service support, sales and research (Irish Times 2011a). FDI now includes logistics, service support and even European or regional headquarters. A cluster of high profile US software and internet firms are now located in Ireland. Google now employs over 2,000 people at its European headquarters in Dublin, in the middle of a fashionably renovated dockland area.

The dependency of FDI employment on the low tax rate has also grown. Traditionally, foreign firms located in Ireland partly because of the low tax on their operations *in Ireland*. Now, high profile American software and internet firms use their Irish operations as a means of ensuring low tax on their operations *across the globe*. Firms use strategies known colloquially as the ‘Double Irish’, the ‘Dutch Sandwich’ and, best of all, the ‘Double Irish Dutch Sandwich’ to move revenues and profits between subsidiaries (IMF, 2013: 47). Thus a firm can have vast revenues but the declared profit – and hence the final tax bill – becomes almost trivial. For example, ‘Google’s operation in Ireland recorded revenues of €15.5 billion, on which it paid Irish corporation tax of €17 million’ (Irish Times,

13 February 2014). Such devices explain how, while the official corporate tax rate in Ireland is 12.5 per cent, US Bureau of Economic Analysis data show that in 2011 US firms located in Ireland in fact paid tax at precisely 2.2 per cent (Stewart 2014).

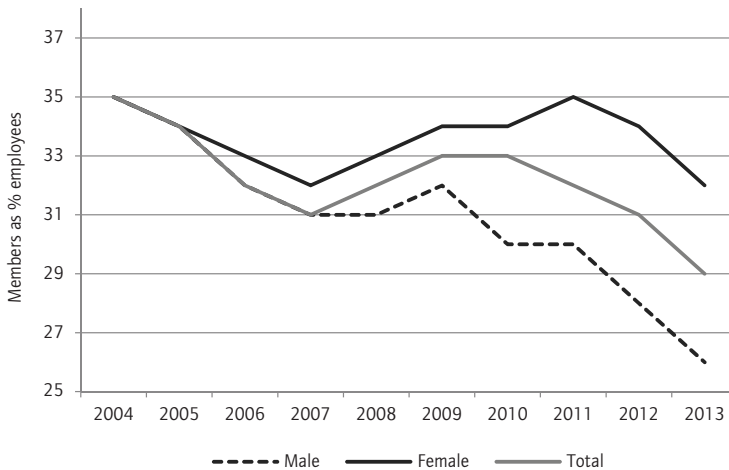
With the crisis unemployment soared, reaching a peak of just over 15 per cent in 2012. Worst hit have been young men. In early 2012 unemployment among males aged 20–24 reached a dismal 35.9 per cent (CSO 2014). The immediate impact on women was somewhat less; the comparable figure for females was 19.9 per cent. Although there has been a slight increase in the number of women apparently withdrawing from the labour market altogether, most women have not only stayed in work but pressure on household budgets means that their earnings are more important than before. However, the gender situation itself is unstable: cuts in state employment impact most on women employed in education and health care, while cuts in services (especially child support) push caring work back into the household – and thus onto women (Barry and Conroy 2013).

More generally, a flexible labour market and a ‘buy not make’ approach to skill creation have ensured that firms have made little attempt to hoard labour through the crisis – in obvious contrast to Germany. Overall earnings have declined. This is clearest in the state sector. At the start of the crisis public sector pay was reduced and a special ‘pension levy’ imposed, even on those on short-term contracts who would never benefit from any public sector pension. Together with tax increases this meant that by 2009 public sector take-home pay was reduced by up to 25 per cent, with the impact greatest in the best paid groups. Meeting the EU/IMF bailout terms in November 2010 led to further cuts in public sector pay and it is estimated that the total public sector pay bill will have fallen by 20 per cent between 2009 and 2015 (Bach and Stroleny 2013). Also as a consequence of the bailout agreement, the government reduced the statutory protection of wages and hours in some low-wage sectors. For those still in employment in the private sector, the impact has been more complex, varying by industry, firm and occupational group. In general, those in the FDI manufacturing and high tech services sector have been affected least and in a few cases wages appear even to have increased. In areas where employment fell most, as in construction, hospitality and retail, wages and conditions have deteriorated sharply for those still in work (Krings *et al.* 2011).

The crisis marks the end of the social partnership that had been seen as a distinctive feature of the Irish model. The only residue of corporatism has been bargaining in the state sector. In June 2010, in the ‘Croke Park Agreement’ between government and the public sector unions, the unions committed themselves to efficiency savings in return for a government promise of no further pay cuts and no compulsory redundancies. In 2013, after controversial debates within the unions, further agreements (‘Croke Park II’ and ‘Haddington Road’) continued the pay freeze and imposed further cuts for relatively highly paid (over 65,000 euros a year) employees. Through these agreements the unions have managed to maintain the principle of ‘no compulsory redundancies’, but little more. Bargaining has been about the implementation of a public sector pay policy on which government had already decided long ago. Quietly but firmly, unions have been excluded from almost all other areas of policy. The unions have largely lost access to government decision-making and there is no attempt from any quarter to recreate the corporatism which was the response to the crisis of the 1980s.

In the final years of the boom women employees became – as in many other countries – more likely to join a union than their male colleagues.

Figure 2 Trade union density, Ireland, 2004–2012



Source: CSO (2014a).

In the crisis union density increased, but is now declining (Figure 2): whereas in 1980 overall trade union density stood at 54.3 per cent, by 2012 it was only 31.2 per cent (OECD 2014). Trade unions are increasingly concentrated in the public sector and it is of course this that explains the growing importance of women. However, media campaigns to portray unions as simply a public sector pressure group have had only limited success: among low and middle income groups unions are, if anything, more popular than before – the problem is simply that most non-unionised employees now simply do not dare to join.

With falling wages and rising unemployment real incomes have fallen, while utility bills have increased, there are new social charges and almost universal tax increases. Average household disposable income was 45,959 euros in 2009 but by 2011 it had fallen to 41,819 euros. In terms of overall income the change seems dramatic when compared to the height of the boom, but is actually rather less dramatic when an only slightly longer time frame is used: average disposable household income in 2011 was about the same as 2006 (CSO 2013a). Nonetheless, most households have been experiencing real difficulties for several years. In 2012 nearly half of all households reported meeting their household bills with ‘some’ or ‘great’ difficulty; over three-quarters had made some cut-backs on expenditure; 40 per cent of all individuals were ‘very’ or ‘some-what’ concerned about their level of debt. The absolute ‘deprivation rate’ (those reporting two or more types of enforced deprivation, such as inability to replace worn out furniture or have an evening out) rose from a low of 11.8 per cent in 2007 to fully 24.5 per cent in 2011 (CSO 2013b).

Radical commentators (for example, Allen 2012), however, deny or downplay one crucial aspect of the Irish crisis: the pain has been *relatively* equally distributed. Conventional indicators of income inequality such as the Gini coefficient or the quintile ratio showed little change as Ireland moved from boom to slump. For example, the Gini coefficient was 31.7 in 2007 and 31.1 in 2011 (CSO 2013a: 3). The conventional poverty rate has hardly changed, for the simple reason that nearly everyone has become poorer. Indeed, 18.5 per cent of the population were ‘at risk of poverty’ in 2005 but only 16.0 per cent in 2011. There are three main reasons for this perhaps surprising situation. First, the lowest paid groups in the public sector have been to some extent protected (pay cuts have hit the better paid significantly more). Secondly, the legal minimum wage has been protected (indeed an earlier cut has been reversed) and remains at the pre-crisis level of 8.65 euros per hour. Thirdly, and most

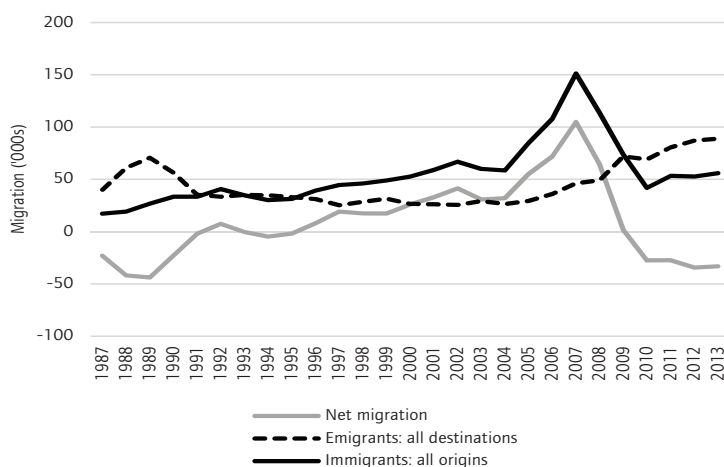
importantly, the welfare state has remained intact. There has been tightening of benefit conditions, and specific vulnerable groups have been hit by state cutbacks (for example, services for children with disabilities, English-language teaching in schools where there are many immigrant children). Nonetheless, basic social welfare rates have remained almost unchanged. State transfers have played an increasing role in maintaining the income of large swathes of the population. Indeed, if all state transfers were ignored, the poverty rate in 2011 would have been fully 50.7 per cent (CSO 2013a).

The real novelty of the crisis is that the financialisation process of the boom and bubble has now shown its dark side. It has contributed to new forms of ‘middle class’ poverty⁵: comparisons with the impact of the great inflation crisis in 1923 Weimar Germany are apt. Here the clearest losers are those who purchased apartments and houses on 100 per cent mortgages at the height of the bubble. By 2011 the value of residential property had fallen nationally by 41 per cent from the peak of 2007 (CSO 2011b). As incomes fell, servicing these mortgages became more and more difficult, while negative equity means that selling the apartment or house is no solution. Despite the recent overall economic improvement, the extent of mortgage arrears continues to rise. As of March 2013 over 12 per cent of all mortgages on principal dwelling houses (PDH) were over 90 days in arrears (Central Bank 2013). Nearly all such mortgage holders are in employment, but the fall in their wages and salaries, coupled with rising taxation, has meant that they are unable to service their mortgages (McCarthy 2014; CSO 2013b). Worst hit are those who have purchased on developments, especially housing estates, which are unfinished – the term ‘ghost estate’ has become a common Irish expression. Such people now face the appalling prospect of repaying loans on property that has become almost worthless.

Unsurprisingly, in this situation emigration is increasing. In 2002 just over 25,000 people left the country; in 2013 89,000 people left. Ireland had returned to its traditional role as a net exporter of people (Figure 3). The recession of the 1980s was the first time that the better educated were more likely to leave. Unlike in earlier decades, Irish social welfare

5. Evidence here remains anecdotal. The main Irish charity, St Vincent de Paul, reported a dramatic increase in applications from ‘middle class’ families. Stories abounded of houses with six bedrooms and twin car ports where the heating was turned off in the winter because there was no money to pay the bills.

Figure 3 Immigration and emigration, Ireland, 1987–2013



Source: CSO (2014b).

benefits were then at British levels, so that the incentive for unskilled emigration was much reduced. Both permanent and temporary graduate emigration has long been normal in Irish society. For example, in a typical boom year such as 2005, over 8 per cent of Irish honours level graduates were working abroad a year later (HEA 2006). Analysis of the 2001 census shows that the higher the level of education, the more likely people are to have lived outside the country (Wickham 2007). This is even more true today: initially, emigrants were disproportionately young and well educated. As the crisis has continued, however, more families and people in mid-career are leaving the country.

At the same time, skilled immigration continues to be crucial for those sectors seen as decisive for economic growth. Despite the crisis, the IT industry has repeatedly complained of significant skill shortages; in summer 2011 Google was complaining that it could not find suitable Irish recruits. Most immigrants during the bubble had been EU citizens from the new member states. This had contradictory consequences once the bubble burst. Paradoxically, legal immigrants were more likely to

be ready to leave because they had unrestricted rights of entry – unlike illegal immigrants, they can come and go as they please, and were not trapped in their new destination, fearful that if they left they might not be able to re-enter. On the other hand, because new member state immigrants had the same social security rights as Irish nationals, their entitlements to welfare support (Jobseeker's Benefit and Jobseeker's Allowance) cushioned them against the immediate need to leave Ireland when they lost their jobs. Furthermore, while very few new member state migrants had ever intended to stay permanently in Ireland, a not insignificant number discovered more personal or quality of life reasons for staying on (Krings *et al.* 2009). The result was that after 2009 the number of new arrivals fell dramatically, but the decline in the new member state immigrant population was much slower. In 2010, there were still over 100,000 new member state nationals at work in Ireland, but now for the first time they had a higher unemployment rate than the host population. There has been some tightening of access to welfare benefits, especially the payment of Family Income Supplement for children not living in Ireland.⁶ Some politicians have also questioned whether new member state migrants should continue to have full access to Irish welfare rights. However, to date there has been no break with the principle that EU citizens cannot be discriminated against in the labour market and in the social security system.⁷

5. Conclusion: six years on

With exports from the FDI sector performing well, its political prioritisation remains untouched. This suppresses any worries about the very narrow base on which it now rests (a few leading US firms in pharmaceuticals, software and electronics) and probably overestimates its R&D contribution. Far from stimulating any rethink of the national development strategy, the crisis turned the reliance on FDI into a national fetish. Bizarrely, not only the Labour Party but even the left-nationalist Sinn Féin has made 'our' corporate tax rate into a symbol of national independence. While personal taxes have risen, the desirability of low

6. Family Income Supplement is a welfare benefit paid to low wage employees who are supporting children: there is no requirement that the children are actually in Ireland, although the claimant's 'habitual residence' must be Ireland.

7. Like other EU states, Ireland delayed access to the Irish labour market for Bulgarian and Romanian citizens.

personal tax rates also remains part of the national political consensus. A socio-economic crisis produced by Ireland's almost pathological commitment to the priorities of Anglo-American capitalism has ended up moving Ireland closer to the United States than to the European Union. Blaming foreign 'European' bankers, cantankerous French politicians and greedy Germans has become a national response across the spectrum of political commentary. The days when the Irish political elite aspired to be model Europeans are now a distant memory. In one sense in particular this Europhobia is bizarre. Ireland has survived the crisis without the collapse of social cohesion that has been seen in Greece partly because of the continued strength of Ireland's most 'European' features. Unions may be weak, but they have managed to ensure that pay cuts within the public sector have been progressive. There has been an increase in insecure employment, but the legal minimum wage has been retained. And above all: the welfare state may have focused on cash benefits rather than services, but universal basic levels of welfare have prevented mass destitution and maintained social cohesion. However, in official media and public discourse increasingly the crisis is blamed not on the excesses of Anglo-American casino-capitalism but on allegedly excessive state expenditure. This is a curious inversion of reality. In fact, the crisis has highlighted the state's ability to protect citizens against the vicissitudes of the market. In Ireland it is precisely the maintenance of the 'European' welfare state, weak and imperfect though it may be, that has prevented social collapse.

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Model or liability? The new career of the 'German model'

Steffen Lehndorff

'We need more Germany in Europe.'

Toomas Hendrik Ilves, President of Estonia, July 2013¹

'Progress – that also means bold reforms to safeguard employment,
as Gerhard Schröder already showed us.'

François Hollande, President of France, May 2013²

'Deutschland, Deutschland über alles!' [to hearty laughter]

John Bowe, board member of Anglo Irish Bank, October 2008³

After being written off ten years ago as 'the sick man of Europe' and poised on the brink of the abyss, Germany is once more being feted as a model. The turning point in its meteoric career was the much-cited 'employment miracle' of 2008/2009: while the German economy was driven by the global crisis into the deepest recession since the establishment of the Federal Republic the effects on the labour market were the mildest in the EU. Thus began what Chancellor Merkel had announced at an early stage: Germany 'emerged from the crisis stronger' (at least politically).

With particularly high growth rates from the second half of 2009 – although they continued only until 2011 – the second part of the success story commenced. While an increasing portion of the euro zone was heading into a further crisis, which is still going on, German policy put on a show that others were keen to emulate. With the motto 'Everyone is the architect of their own fortune' the German government declared its policy and that of its predecessors to be a model for the rest of the EU

1. FAZ, 10.7.2013; on the occasion of a state visit by German President Gauck to Estonia Ilves called on Germany to 'take a more decisive lead in Europe and to be less willing to compromise with the indebted states of southern Europe'.

2. Le Monde, 24.5.2013 (http://www.lemonde.fr/europe/article/2013/05/23/a-leipzig-hollande-loue-les-reformes-menees-en-allemande_3416355_3214.html).

3. FAZ, 26.6.2013; the quotation comes from the recording of a telephone conversation with chairman of the board David Drumm, the topic of which was how urgently needed deposits could be obtained from large investors to shore up the struggling bank.

and especially the euro zone. In the media, both in Germany and abroad, it has become part of the conventional wisdom that German success originated in Agenda 2010. This is how the world champion exporter managed to export even Hartz IV, pensions at 67 years of age and the debt brake, although coercive measures were needed to get people to buy into these innovative products. But is there any truth in this success story?

1. Leading up to the crisis: the pathogenic man of Europe

The core of what was long described as the German variant of ‘coordinated’ or ‘Rhenish capitalism’, was a combination of economic dynamism and relatively low social inequality. Up to around 20 years ago institutions such as the system of industrial relations, labour law and the welfare state enabled the economy as a whole and large segments of the population to benefit from the success of the global market-oriented industries based on high added value and quality production and sustained by ‘patient capital’ and well paid employees. However, after the historic turning point of 1989/1990, the overnight monetary incorporation of eastern Germany and the subsequent long-term unemployment the German model, at least to domestic observers, was portrayed in ever more sombre colours. One leading economist very popular among journalists described Germany as the ‘sick man of Europe’ and asked whether ‘it could still be saved’ (Sinn 2003). This was when the political and economic upheaval initially introduced surreptitiously in the 1990s reached its zenith – or nadir – and in particular with ‘Agenda 2010’ went even further than the adjustments to the neoliberal mainstream made in many other EU countries. As a result, the German model, on the eve of the great crisis of 2008/2009, offered something new: a revived and high-performance export industry in an environment of social and institutional disintegration and fragmentation.

This constellation helped to pave the way for the crisis. It is one of the main reasons for the emergence of the current crisis in the euro zone.

1.1 Profiting without investing: a business model

The alpha and omega of Germany’s economic success is the strength of its export industry. It also provides the basis for the self-confidence

displayed by the German government and the mainstream media: why should a country give ground when it's doing so well – the others should simply try harder! In fact, German industry's export success is based primarily on the high specialisation and product quality especially of capital goods, the strong orientation towards customer service and the flexibility and qualifications of the employees, all factors embedded – at least hitherto – in comparatively strong medium-sized (*Mittelstand*) ownership structures and a broad system of institutions ranging from occupational training to codetermination, as well as in a culture in which technical work is appreciated (for more details see Lehnendorff *et al.* 2009). It is thus too simple to claim, as critics of the German economy occasionally do, that the economic imbalances in Europe stem from German 'wage dumping'.

But what is the problem, then? In order to understand what is at stake, both sides of wages – their role as a cost factor and in terms of demand in the national economy – should be considered. Let's start with the first.

The imbalances in the euro zone are basically connected to the fact that the competitiveness of the German economy, with its product-related fundamentals, was *supplemented* from the beginning of the 2000s by a fall in unit labour costs in comparison with the other EU countries. Average real wages in Germany fell, while labour productivity rose in relation to the EU average, which enabled particularly low price increases far below the euro zone average, as well as the ECB's target inflation rate. Even in industry unit labour costs in Germany fell up to 2008 much more than in any other country in the euro zone, with the exception of Finland (on what follows see Herzog-Stein *et al.* 2012). On top of this comes the fact that wages in the private services sector in Germany are on average 20 per cent lower than in industry (unprecedented in the EU), which means that many pre-services for industry are extremely cheap. The Bundesbank (2011: 17) was thus certainly right to claim that German export success also gained 'impetus from improvements in price competitiveness'.⁴

It can reasonably be pointed out that demand for many German export products does not depend primarily on price. It should be borne in mind,

4. The European Central Bank (ECB 2011) estimated the improvement in Germany's price competitiveness compared with the major global trading countries in the period 1999 to the beginning of 2011 at 16 per cent (basis: GDP deflator). The only other EMU countries with positive values are Finland (6.4 per cent), Austria (4.6 per cent) and France (3.2 per cent)..

first, that this does not apply by any means to all export branches.⁵ However, there is no doubt that in particular in automobiles and machine building, which account for around one-third of German goods exports, the price elasticity of demand is relatively low. Thus although unit wage cost advantages in the metal industry were not reflected in falling prices subsequent to 2000, while at the same time competitors in other euro-zone countries raised export prices – at least in relation to the sector average – profits increased (IG Metall 2010). The Bundesbank (2011: 33), too, pointed out that part of the relevant cost benefits ‘were apparently used to increase profit margins’. I shall return to this important point in due course.

The other side of the coin was the domestic economic imbalance, which indicates the importance of falling average wages for the development of economic demand in the German economy. From the end of the 1990s the key issue was the level of labour costs. Bringing them down in order to boost the competitiveness of the German economy was the focus of all public ‘debates’. The supposed imperative of lowering labour costs was never questioned, whether in relation to pension reform, decentralisation of collective bargaining or tax policy. However, in contrast to what had been prophesied by the neoliberally inclined main actors in the economy and politics no impetus was discernible from falling wages and labour costs for either investment or growth. Germany’s special role within the EU is reflected in the GDP growth rates, the price level and disposable household income since 2001: German rates of increase were below the EU average almost continuously (Table 1).

As a consequence, in the period between 2001 and 2008 three-quarters of German economic growth was attributable to the export surplus, while domestic demand contributed only a quarter (Priewe and Rietzler 2010: 64). The weak wage development thus hindered both a transfer of the growth impetus from the export boom to the domestic market and also a boost to imports, which would have enabled Germany’s trading partners abroad to benefit from its export-induced growth impetus (Joebges *et al.*

5. For example – to give an extreme instance – the particularly crass social and wage dumping in German slaughterhouses caused a public outcry in German public opinion. German media, however, were less concerned with the external effects of this: jobs are at serious risk especially in the Danish, but also in the French meat industry; in Denmark there has been a heated debate about the maintenance of wage standards (Czommer and Worthmann 2005; Refslund 2012).

Table 1 Real growth, inflation rate and disposable household income: Germany and EU27, 2001–2008 (annual growth rates in %)

	2001		2002		2003		2004		2005		2006		2007		2008	
	DE	EU	DE	EU	DE	EU	DE	EU	DE	EU	DE	EU	DE	EU	DE	EU
Real GDP	1.2	2.0	0.0	1.2	-0.2	1.3	1.2	2.5	0.8	2.0	3.2	3.2	2.5	2.9	1.3	0.8
Inflation	2.0	3.2	1.4	2.5	1.0	2.1	1.7	2.3	1.6	2.3	1.6	2.3	2.3	2.4	2.6	3.7
Disposable income	2.1	3.3	-0.4	1.6	0.5	1.6	0.2	1.4	0.6	1.7	1.0	1.7	-0.2	1.6	0.6	1.5

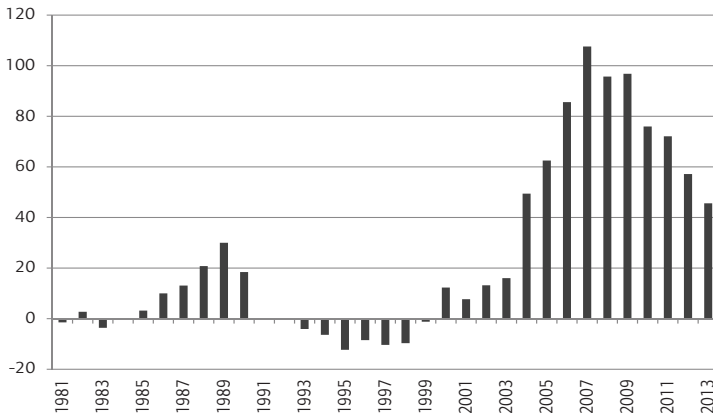
Source: OECD Country Statistical Profiles.

2010: 10). Herzog-Stein *et al.* (2013: 17) show, on the basis of alternative model calculations, that higher wages would not have adversely affected either employment or economic growth: 'The stronger domestic dynamic would have compensated for the weaker foreign demand and growth and employment would have been higher with such a wage policy.'

The domestic weakness of Europe's largest economy was the main source of the external imbalances that led to the overt crisis in the euro zone. While in previous decades the exchange rate adjustment mechanism would have made it possible for weaker economies to compensate on occasion for such developments, since the founding of the monetary union two-fifths of Germany's foreign trade now no longer had to fear such action. Germany's business model now flourished in the way it had been hoping for since the signing of the treaties on European monetary union in the 1990s. This paid off, as the impressive rise in current account surpluses proved only a few years after the introduction of the euro (Figure 1).

To sum up, the criticism often formulated by critical observers that Germany exports too much tends to divert attention from the core problem. It makes more sense to emphasise the other side of the coin: *Germany imports too little*. In order to avoid misunderstandings it would thus be better to criticise the *import deficit*, rather than the export surplus. Incongruously – and uniquely – the strongest economy in the euro zone drove down average domestic wages, thereby making itself one-sidedly dependent on exports (with important side-effects on profitability), while at the same time depriving its competitors of the opportunity, due to the weakness of its domestic market, to compensate by increasing

Figure 1 Germany's current account balances with the countries of the euro zone (€ billion)



Source: Bundesbank; author's own graph.

their own exports to Germany. *Making profits without investing* – this is the common denominator that sums up the German business model in the euro zone.

The upheavals in the German economic and social system – which reached their apex with Agenda 2010 – have contributed substantially to this dubious success.

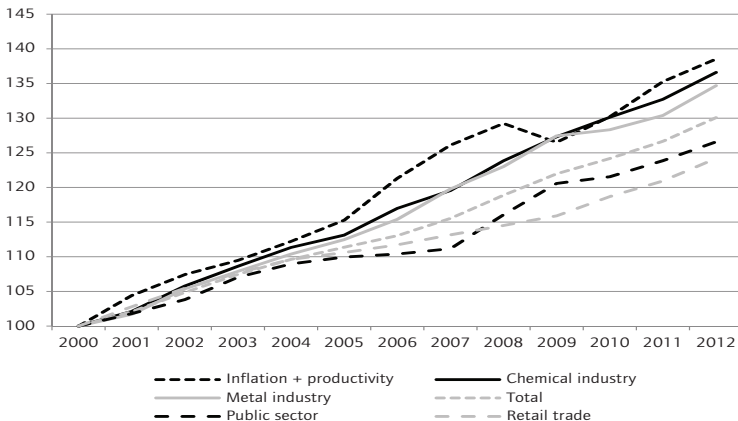
1.2 'Hartz IV is poisoning Europe'

What lies behind the weak wage development in Germany, which is often referred to as 'wage moderation'? Are the trade unions letting themselves be swayed in their wage policy, as both domestic and foreign critics occasionally suspect, by an imperative to boost the price competitiveness of export industry? Although a competition-oriented corporatism certainly exists, it is itself part of a more complex problematic. Attempting to understand this brings us to the heart of the upheavals of the German employment model.

A glance at the development of collectively agreed wages from 2000 to 2012 (Figure 2) yields a perhaps surprising realisation. In the metal and chemical industries, of all places – in other words, in the two economic branches exposed most intensively to international competition – collectively agreed wages and salaries have risen most strongly. It is true that even the comparatively assertive trade unions in these sectors were unable up to 2008 to take full advantage of the so-called distributionally neutral leeway defined as the sum of price rises and aggregate productivity growth (I shall go into more detail concerning subsequent years in due course). The main reasons for the low average wage rises, however, lay in branches – such as retail trade and public services – that are not exposed to international competition or only to a small extent.

What weighed down the Vereinigte Dienstleistungsgewerkschaft (ver.di – United Services Union) in public services collective bargaining was the tax reforms of the SPD/Greens government, which resulted in considerable loss of revenues for public finances (in the middle of the previous decade they had amounted to more than 40 billion euros a year; Truger and Teichmann 2010). The massive pressure for spending cuts thus unleashed directly affected the wages (as well as working time) of

Figure 2 Development of collectively agreed wages in selected branches, 2000–2012 (2000 = 100)



Source: WSI-Tarifarchiv.

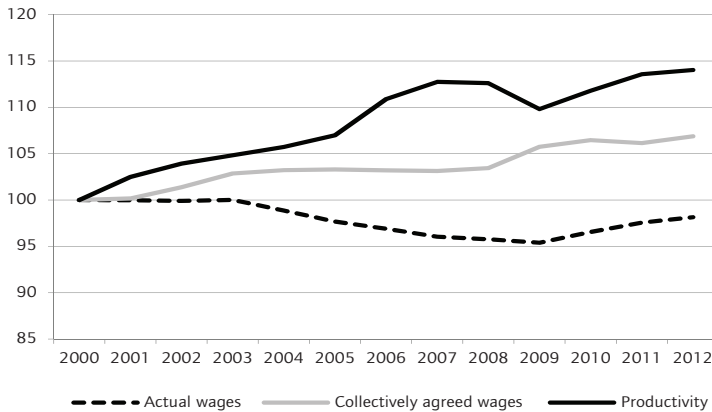
public service employees. An important side-effect of this pressure was the exit from the public employers' collective agreement by the federal states hit hardest by declining tax revenues. It was thus no accident that collectively agreed wage rises in public services were among the lowest in the major economic sectors. This was owing not least to trade union fragmentation: broad swathes of public employees now had to seek salary increases without being able to rely on, for example, the propensity to strike of the refuse collectors. The changes in the institutional framework and the political balance of power are inextricably linked.

All these are features of the first structural break, namely the erosion of the power political constellation and institutional architecture within which the so-called convoy principle has traditionally functioned in German collective bargaining. The tacit conditions for the success of that 'wage formula', to which the industrial trade unions continue to orient themselves in their bargaining policy, have been unhinged at the level of both primary distribution (collective bargaining) and secondary distribution (welfare state compensation mechanisms). As a result, the real problem facing the trade unions is the loss (or relinquishment) of political influence over the implicit conditions of a more solidaristic wage policy ('convoy principle'), including in particular tax policy and the cornerstones of labour market regulation (described below). The drifting apart of collectively agreed wages thus conceals both a power political and an institutional break, which probably can be made good by means of collective bargaining only to a limited extent.

The second structural break is expressed in the fact that real wage increases from 2000 until the crisis were only half as high as collectively agreed wage increases (nominal 12.7 per cent in contrast to 23.6 per cent) so that real wages per capita fell by over 4 per cent (Unger *et al.* 2013; Figure 3). This was due to the following:

- the weakening of the trade unions: net trade union density has fallen from around 30 per cent in the mid-1990s to around 19 per cent today (ICTWSS Database 2013);
- the abatement of collective agreement coverage: in 1996 70 per cent of employees in western Germany worked in companies covered by branch collective agreements, but by 2012 this had fallen to 53 per cent (in eastern Germany the proportion fell from 56 per cent to 36 per cent; Ellguth and Kohaut 2013); according to the Federal Statistical Office (Statistisches Bundesamt 2013a) in 2010

Figure 3 Collectively agreed and actual real wages per employee, 2000–2012 (2000 = 100)



Source: WSI-Tarifarchiv.

- even including company agreements only 55 per cent of employees were working in companies covered by collective agreements; the systematic dismantling of the option of the government declaring branch collective agreements to be generally binding by the employers' umbrella organisation (Schulten and Bispinck 2013);
- many local deviations from collective agreements since the early 2000s. In particular, in the metal industry wage cuts and prolongations of working time would have hollowed out the system of collective agreements if the trade unions had not counteracted them by eventually mobilising the membership (Haipeter 2013).

Besides these institutional changes – *third – institutional foundations* have also started to show cracks. Two changes in particular are important here: on one hand, the outsourcing of pre-services, by means of which ever broader segments of industry and services are becoming subject to lower working conditions and wage standards; on the other hand, the privatisation of public services. Thus in line with the EU services directive, for example, massive low wage competition became a feature of postal services. Needless to say, neither outsourcing nor privatisations are particular to Germany. However, in connection with the

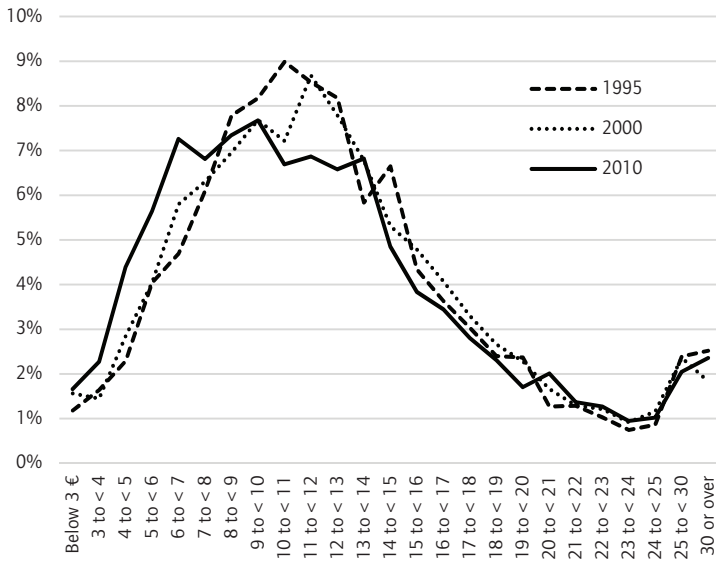
abovementioned institutional upheavals – especially the widening gap between wages in industry and in services, as well as the lack of generally binding collective agreements – they are reinforcing the dampening effect on labour incomes.

The *fourth* and particularly onerous stumbling block on wage development is the *changes in the architecture of labour market regulation* since 2003 (on the following see Bäcker *et al.* 2011 and Knuth 2014):

- The massive reduction in unemployment insurance in favour of a system with means testing that requires that offers even of jobs with low standards must be accepted has had an intimidating ripple effect in broad segments of the labour market (Erlinghagen 2010).
- The German government paved the way for dumping collective agreements with the de facto abolition of the European equal pay principle in temporary employment. From 2003 to 2008 the number of temporary employees doubled to almost 3 per cent of all employees subject to social security contributions. Temporary workers on average earned around half as much an hour as standard employees in 2006.
- Strong impetus for the extension of atypical employment was given, on one hand, by public subsidies for low wages within the framework of Hartz IV and, on the other – and frequently in combination with it – by the promotion of mini-jobs with pay of up to 450 euros. Around 14 per cent of all dependent employees – most of them women – are now exclusively in marginal employment (even not including schoolchildren, students and pensioners the figure is around 9 per cent) and 84 per cent of them are on low wages (Weinkopf 2012).

Bäcker *et al.* (2011: 48) sum up the most important effects of these labour market ‘reforms’ as follows: ‘since the introduction of the ‘Hartz reforms’ pressure has increased to accept employment even under the poorest conditions as regards low wages, temporary work, fixed time employment, part-time work or mini-jobs’. As a consequence of these upheavals since the mid-1990s a large low wage sector has emerged; on the eve of the crisis 22 per cent of employees earned less than two-thirds of the median wage (Figure 4). Particularly noteworthy is the fact that only a minority of them – around a fifth – have no occupational or academic qualifications. The justification of low wages often presented – that they offer low qualified people a chance to enter the labour market – is thus highly dubious.

Figure 4 Distribution of hourly wages, Germany, 1995/2000/2010*



* Note: Main job (if not available, second job), adjusted for inflation (base = 1995), including schoolchildren, students and pensioners; share of all dependent employees (%)

Source: IAQ calculations (Thorsten Kalina) on the basis of SOEP.

One aspect is worth emphasising in this context: the significance of the mini-job regulation, which has contributed substantially to the growth of the low wage sector, is closely related to the maintenance of the conservative welfare state which partly compels and partly promotes limited participation by women in working life. The lack of child care facilities makes it difficult for many women with young children to resume work fairly quickly, while the tax and social contribution system makes unequal distribution of employment income between married couples financially attractive (Bosch and Jansen 2010). Even though this system, which is still stuck in the 1950s, is increasingly coming under criticism and some modernisation has taken place (such as the introduction of a parental allowance on the Swedish model) its stability stands in marked contrast to the neoliberally inspired reforming zeal in other areas. The extent of this stability is reflected in the retention of a benefit for parents *not* using child care, as well as in the stubborn defence of tax splitting for married couples. The precaritising effect of the upheavals in the institu-

tional system of the German labour market is massive also because of the reciprocal action of these 'labour market reforms' and the conservative gender model in the German welfare state.

The fall in (price adjusted) *average* wages among all employees in the 2000s up to the crisis is thus not to be attributed primarily to 'wage moderation' on the part of the trade unions in export industries, but rather to the widening gap between collectively agreed and actual wages as a consequence of the upheavals in the employment system. 'Hartz IV is poisoning Europe', as one commentator succinctly put it in the sadly now defunct *Financial Times Germany* (Münchau 2010).

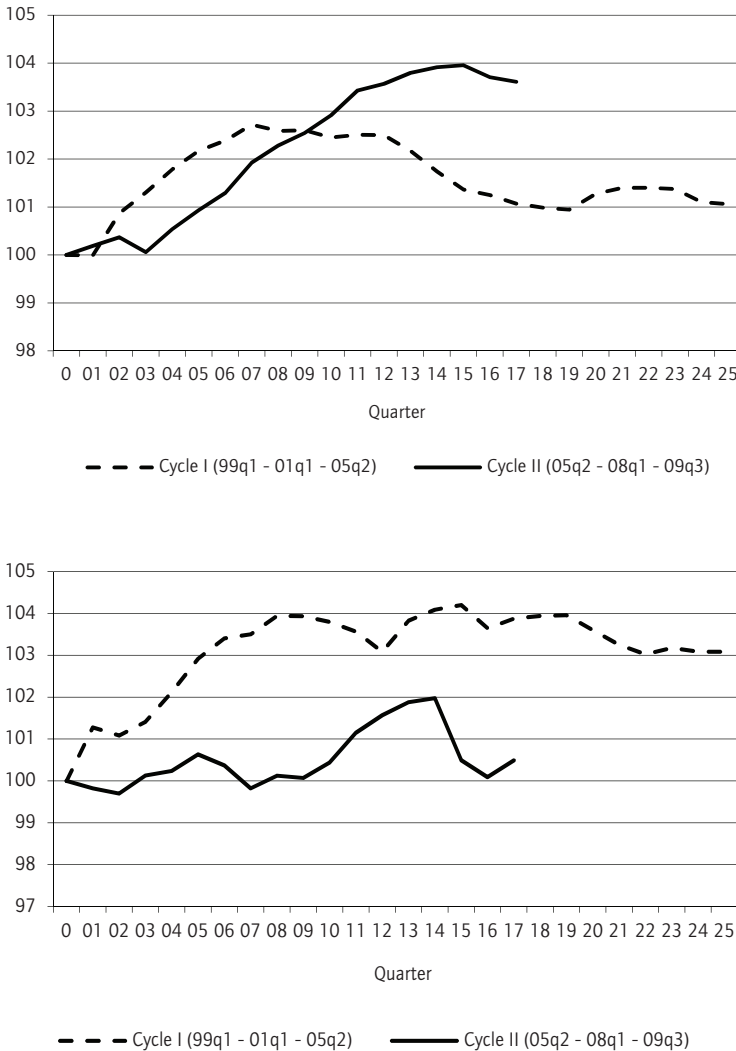
On the German government's own account of the matter, which public opinion has largely bought into, things are rather different. Thus Chancellor Merkel, at a global economic forum in Davos, announced that the 'structural reforms' implemented in Germany 'under the name "Hartz IV"' had 'led to a massive improvement in the labour market' (Merkel 2012). Let us therefore briefly examine what evidence exists that this is how things were before the financial crisis hit.

1.3 Under way to an 'employment miracle'? The Agenda myth

In 2005 a recovery began from the prevailing stagnation and recession. Employment rose. If the increase in employment from 2005 had anything to do with implementation of Agenda 2010 then employment growth ought to have been even stronger after the 'labour market reforms' than before them. However, as Herzog-Stein *et al.* (2013: 9) have shown, by comparing the three succeeding growth cycles, this was not the case: 'German economic growth was one of the lowest in the euro area for a period of ten years. These figures do not bear out the alleged success of supply-side policy, rather its failure.' The stronger overall employment growth in the years before the great financial crisis in comparison with the growth phase at the end of the 1990s up to 2001, in turn, was due solely to the somewhat longer upturn up to 2008 (Figure 5a).

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6. Burda and Hunt (2011: 32) reach a similar conclusion, despite the fact they are rather uncritical with regard to Agenda 2010. According to their calculations employment growth was comparatively halting in the years before the crisis, which they explain by a preference for longer working hours in place of new hires. However, according to these authors, this led to the creation of the working time buffer that helped to stabilise employment during the crisis.

Figure 5 Development of employment and real wages in comparison with the preceding economic cycle, 2005–2009 (beginning of respective business cycle = 100)



Source: Herzog-Stein *et al.* (2013).

The employment intensity of growth up to 2008 was even a little lower than in the preceding upswing.⁶ However, the very unusual stagnation in average real wages during a period of economic growth is striking (Figure 5b). No employment effect of the labour market reforms is therefore discernible. 'A comparative improvement came only with the active demand-side policy implemented to cope with the crisis in 2008/2009' (Herzog-Stein *et al.* 2013) and wage development in the ensuing upturn.

However, the number of registered unemployed fell back sharply after the 'Hartz reforms'. The labour market statistics offer considerable material for debate, but according to the Federal Employment Agency between 2006 and 2009 switching from employment to unemployment increased to the same extent as switching from unemployment to employment – in other words, overall there was a 'higher degree of change between employment and unemployment' or an 'increasing unemployment dynamic' (BA 2011: 14f). In Bosch's (2013) estimation this primarily reflects the greater emphasis on external flexibility in company human resources policy based on fixed-term contracts and temporary work. Any additional employment was therefore supplied more than previously from among the unemployed rather than from newcomers to the labour market. At the same time, older employees retired later because claiming unemployment benefit 'as part of a passage to early retirement' (Knuth 2014: 6) had been made almost impossible and they had to avoid or at least mitigate the losses ensuing from the pension reforms.

Also noteworthy in this context is the fact that during the same period the number of long-term unemployed and of recipients of the means-tested 'unemployment benefit II' fell only slightly. On the other hand, the number of working poor rose considerably. Switching between unemployment and – frequently insecure – low-income jobs has become much brisker. The unemployed do everything in their power to avoid sliding into the clutches of Hartz IV – a fate to which the adverse changes in the criteria concerning what counts as a reasonable job also condemn them – while those with relatively secure jobs cling on to them for dear life and are willing to make greater concessions with regard to wages in the face of intimidation due to the labour market reforms (Knuth 2014: 6). Lowering unemployed people's 'level of expectation' was one of the express aims of Hartz IV right from the start – and it was achieved. A 'paradox of employment and poverty' developed (Arbeitsgruppe Alternative Wirtschaftspolitik [Alternative Economic Policy Working Group] 2013: 20): more employment went hand in hand with a rise in the risk of poverty.

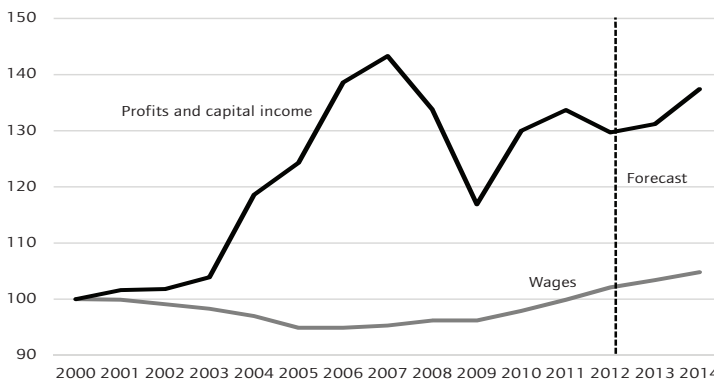
Even among those cheering on the Hartz reforms, some, such as ZEW economist Holger Bonin (2013: 150), have come to the conclusion that 'the structural improvements brought about by the reorientation of labour market policy alone' could not explain the rise in employment since 2005: 'Presumably the strongest support came from the restoration of international competitiveness due to many years of wage moderation ... Furthermore, the emergence of a low-wage sector resulting from the greater employment pressure imposed on the low qualified unemployed subdued the growth of average unit wage costs.'

The sole undisputed effect of the Hartz reforms was thus the pressure on wages and the powerful additional impetus for the low-wage sector. The question remains, what happened to the rising capital income that was a corollary of falling average wages?

1.4 What to do with the money? Symbiosis of core and periphery

In contrast to stagnating and in some places even falling average wages, as already mentioned, profits were rising significantly (Figure 6). The share of profits in GDP rose by 9 percentage points from the beginning of the 2000s to the eve of the crisis. The dynamic of rising inequality was among the strongest in the EU (Schäfer 2012; ILO 2010).

Figure 6 Wages and profits, Germany, 2000–2012 (2000 = 100)



Source: Federal Statistical Office, National Accounts; Prognosis: Economic Outlook Autumn 2013, price adjustment by means of the consumer price index; graph: ver.di economic policy department.

On top of all this, secondary distribution did much less than had previously been the case to attenuate the changes in primary distribution. The reasons for this included the already mentioned tax reforms introduced by the SPD-Greens government, which had considerably lowered the top rate of income tax, together with taxes on capital income and company profits. As a result, inequality shot up during the growth period of 2004–2008: moderate falls in net wages were in sharp contrast to a rise in net capital incomes (incomes of private households from business activities and assets) of around 20 per cent (Brenke 2011).

Due to weak economic growth, however, only a small part of rising profits could be used for domestic investment. Money capital that could not be invested profitably at home had to find investment opportunities beyond domestic manufacturing and consumable services. And it succeeded: numerous deregulations of the financial sector (Huffs Schmid 2010) had opened the doors for German profits and investment income to participate actively in a booming global financial market bubble and in particular the financing of strong growth driven by partly private, partly public debt in Europe's deficit countries. German investors were among the largest foreign creditors of the indebted US private sector;⁷ and German banks were the largest creditors of partly private, partly public debtors in Greece, Ireland, Portugal and Spain (Bofinger 2010; Lindner 2013).

An analysis by the Bank for International Settlements (Ma and McCauley 2013: 8 and 13) comes to the conclusion in relation to Germany that '[t]he fruits of wage moderation and labour market reforms were not invested domestically but instead funded the accumulation of net foreign assets', which on this account did not involve an increase in direct investment, but a massive boom in lending abroad. It was thus only a minor journalistic exaggeration when a commentator in the British Guardian newspaper declared: 'Germany blew the bubbles that popped up in the rest of Europe' (Chakraborty 2011). It stands to reason that the bursting of this bubble resulted in considerable losses among German investors and banks, too (Herzog-Stein *et al.* 2013).

7. A typical anecdote is given in Martin Lewis's thrilling account (2010: 90) of the US subprime market boom in the years leading up to the crisis. A hedge fund manager, who believed that the bubble would soon burst and gambled on that eventuality, recalled a conversation with a New York trader at Deutsche Bank (who has now founded his own hedge fund): 'Whenever we asked him who was buying this junk he only said "Düsseldorf".' This evidently meant IKB, which was one of the first victims of the bursting of the speculative bubble in 2007.

The German economy is no more a victim of the euro-zone crisis than of the global financial crisis. On the contrary, it was heavily complicit in preparing the ground for these crises. But how did it manage to overcome the 2008/2009 crisis so rapidly and – to all appearances at least – emerge from it stronger than ever? Curtains up for the real 'employment miracle' and its true causes.

2. A succession of crises: the mislabelled success model

The fact that Germany is currently being held up as a model can be traced back to the much lauded 'German employment miracle' since 2008/2009. The truly astonishing stability on the labour market during the financial crisis was the main condition of the rapid economic recovery from the third quarter of 2009 and the ensuing growth in employment in the following years. On one hand, for the first time in many years stronger economic impetus came from the domestic market; on the other hand, on this basis industrial companies were able to react most quickly to the initial global economic recovery. Furthermore, in combination these developments were such a balm for crisis-hit state budgets that Germany was able to avoid what other – sometimes even less indebted – countries were obliged to do: introduce drastic austerity programmes. Exaggerating only slightly one can say that the growing power of the German government in the EU is largely based on the fact that – albeit to a modest degree – what was forbidden to other countries happened in Germany.

We shall now look in more detail at this successful mislabelling and the paradoxes arising from it in Germany's recent economic development.

2.1 Rediscovery of traditional strengths

The revival of old virtues began with the sudden – if only temporary – setting aside of numerous neoliberal dogmas. Almost overnight, counter to the relentless mantras that had previously prevailed, extensive economic stimulus programmes were implemented. While in the years before the crisis economic growth was hindered by cuts in public spending which matched lower tax revenues due to tax reforms, the temporary change of course in financial policy in 2008 and, especially, 2009 was a considerable impetus to growth (IMK Arbeitskreis Konjunktur 2011).

The Bundestag elections in 2009 were imminent and any hesitancy about rescuing the ‘real economy’ would have been a political disaster for the government parties in the face of the billions paid out and provided as sureties to banks.

The economic stimulus programmes met with the active cooperation of both the employers’ organisations and the trade unions. Above all at the national level an informal ‘crisis corporatism’ emerged, accompanied by a reactivated social partnership at all levels (see Urban in this volume). The biggest direct effect of this recovery was the prevention of a massive fall in employment in crisis-ridden industry. It is true that considerable numbers of temporary workers were made redundant, but in the labour market overall this fall in employment was more than offset by employment gains in other branches. The reference to temporary work makes it clear, however, that crisis corporatism and reactivated social partnership could include recourse to external flexibility when it came to protecting core workforces. However, the main emphasis was on internal flexibility. This was something new – or rather, new once again. Only a few years beforehand, during the preceding phase of recession and stagnation, many companies had thinned out their workforces to such an extent that they struggled with staff shortages when the economy revived. This was still fresh in the memory and now even considerable productivity losses were accepted in the short term in order to retain skilled staff.

The most striking expression of this about-face was the considerable reduction in per capita working time (OECD 2010). It was based on the mobilisation of various resources of the German employment model, partly new, but primarily traditional strengths, rediscovered in the crisis, which had survived the abandonment and upheavals of the preceding years (for more detail on what follows see Bosch 2011 and Lehndorff 2011). More to the point, since the mid-1990s increasing *external* flexibility had been one of the core neoliberal dogmas of employment policy; this was thus also one of the guiding principles of the SPD-Green ‘labour market reforms’. What rescued the German labour market in the crisis, however, was precisely the opposite: the reactivation of *internal* flexibility.

Key to the revival of internal flexibility was short-time working, at levels not seen since the mid-1970s (Herzog-Stein *et al.* 2010). But other working-time measures contributed as much if not more to reducing the volume of work: the reduction of positive balances on working-time

accounts, which in previous years had sometimes grown considerably; the reduction of overtime; and the use of collective agreements to ensure employment (Bogedan *et al.* 2011). Above all, the various forms of cuts in individual working time had even more of a massive effect on total volume of work than (collective) short-time working (Fuchs *et al.* 2010; Groß 2013).

One resource of the German employment model that has received less attention, but which helped to prioritise internal flexibility during the crisis, despite its problems, was the occupational training system, whose strategic significance for both companies and employees in the crisis was never called into question (Voss-Dahm 2011). One direct effect of this was that the unemployment rate among young people initially did not rise sharply and up to 2011 even fell below its level in 2008.

However, the upheavals of the preceding years were also discernible in the crisis. The rapid and sharp fall in temporary work indicated how far the dualisation of the labour market has gone. We have only the brevity of the crisis to thank for the fact that this was not reflected in the overall balance of labour market processes. Not so obvious but just as important is the dualisation in the character of the much praised working-time flexibility. In the crisis it was often found that being able to reduce working-time buffers was of great benefit, although previously these buffers had been built up, especially in the form of high balances on working-time accounts. Thus in the metal industry between 2003 and 2008 average actual working time of full-time employees rose by an hour, while the number of core employees had initially been reduced further (Lehndorff *et al.* 2010). Many companies clearly found it easier in the crisis to avoid lay-offs because during the previous growth phase they had been able to a considerable extent to avoid new hires by extending working time (Burda and Hunt 2011). Although the reduction in positive balances on working-time accounts that this made possible did not provide them – in contrast especially to short-time working – with direct cost savings the weak employment development and the increasing social inequality in the pre-crisis years had swelled the profit cushion, which – and this was the price that companies had to pay – now had to be sacrificed, at least in part, to economic and social stability.

What happened in 2008 and 2009 can be summed up as follows: *while before the crisis the upheavals in the German employment model had contributed actively to the emergence of European and global economic*

imbalances the stabilisation of the labour market and the economy during the crisis was owing to a reactivation of precisely those elements of the German model that had survived the neoliberally inspired zeal for demolition. In Germany, at least, this triggered a political dynamic – guided by Merkelian adaptability – that could not easily be dismantled again as economic recovery set in from the second half of 2009.

2.2 Zigzagging in the ‘long shadow of the 2000s’

The new inconsistency was soon reflected in economic developments. As radical and sudden as the descent into crisis was, the upturn as early as the second half of 2009 was every bit as rapid and robust. Many German industrial companies had, as it were, bided their time and kept their motors running. When foreign demand rose again in the third quarter of 2009 qualified workers were still on board, short-time working came to an end, temporary workers who had been released were rehired and empty working-time accounts were restocked. The economy was good to go and many believed that things could continue as they had been before the crisis.

But it wasn’t going to be so easy. In spring 2010 the great crisis of the euro zone broke out and the measures taken to combat it – mainly at the urging of the German government – turned a tractable regional disaster into a conflagration. More and more of the euro zone was gradually driven into recession again, including countries previously considered neoliberal success stories, such as the Netherlands.

The export world champion could not remain unscathed by all this. As can be seen in Figure 1 the current account surplus in relation to the euro countries, first with the global financial crisis and then once more with the outbreak of the euro zone crisis fell significantly (on what follows see IMK-Arbeitskreis Wirtschaftspolitik 2013; IMK/OFCE/WIFO 2013; Deutsche Bundesbank 2013a). However, initially it was possible to make up for this loss by means of export growth, especially with Asia and the Americas, an uncertain workaround not least because the recession in Europe also affected the global economy. Nor should it be forgotten that the euro zone is, with a share of just under 40 per cent, still the largest export market for the German economy, dwarfing those of the United States (8 per cent) and China (6 per cent).

Table 2 Development of GDP and the growth contributions of its components, Germany, 2009–2013

	2009	2010	2011	2012	2013	2014
Real GDP	-4.7	+3.7	+3.3	+0.7	+0.4	+1.8
<i>Growth contributions of structural components (ppt):</i>						
Exports	-2.9	+1.5	+0.7	+0.9	-0.2	-0.5
Domestic demand	-1.8	+2.3	+2.6	-0.3	+0.6	+2.3
Private households	-0.1	+0.4	+1.3	+0.4	+0.5	+ 0.9
State	+0.5	+0.3	+0.2	+0.2	+0.1	+0.2
Capital investments	-1.9	+1.0	+1.2	-0.4	-0.1	+1.2

Note: * 2014 forecast.

Source: IMK.

It could therefore come as no surprise that, after the rapid upturn in 2010/2011, growth rates fell again in Germany, too. However, the pattern of Germany's economic development since 2009 has not entirely matched the one familiar from before the crisis. Let us recall that, as already mentioned, between 2001 and 2008 around three-quarters of the relatively low growth of around 1.2 per cent a year, on average, was based on exports and only a quarter on domestic demand. In three out of the four years after 2009, by contrast, domestic demand contributed more to growth than the export surplus (Table 2).

If balanced economic development is to be achieved in Germany and Europe, however, this shift is still much too weak and the import deficit remains high. Nevertheless, the stabilising influence of consumer demand on the domestic market should not be underestimated. On top of that comes public-sector demand that, although weak, at least does not play a negative role. Here a positive sum game comes into play that is prohibited for other countries with reference to the alleged need to reduce new borrowing right away: because of the increasing employment and rising wages and salaries tax revenues are also increasing. The positive sum game is also supported by a kind of crisis dividend, namely the interest benefits arising for the German budget from the euro crisis. The so-called 'safe haven effect' made German government bonds such a desirable form of investment in the wake of the euro crisis that their average interest rates have fallen from just under 5 per cent before the

crisis to 3 per cent in 2012. This accelerated a tendency observed since the late 1990s, namely that Germany, despite increasing public debt, has had to devote an ever smaller portion of public spending to interest payments: the net interest burden in 2012 was below 2 per cent, a low value last seen in the early 1980s (Bundesbank 2013b: 53). The German state is now borrowing, roughly speaking, at no cost, in real terms. One can scarcely do better out of an alleged 'public debt crisis'.

Nevertheless, 'the long shadow of the 2000s' (Bispinck 2012) still lies on the labour market. The proportion of employees and households on low incomes was still at the pre-crisis level in 2011 (and, depending on the method of calculation, even a little higher; Kalina and Weinkopf 2013). The number of workers in temporary employment exceeded the pre-crisis peak as early as 2010 (BAP 2013); working time has also returned to the pre-crisis level (Franz and Lehndorff 2012). The number of those in work continues to rise and even the number of full-time employees rose again, but the significance of precarious employment has not diminished. All in all, Germany's economic and social development since 2009 can best be described as zigzagging. This can also be discerned in the development of average real wages, which have risen overall since 2009, but from time to time have also fallen slightly (Federal Statistical Office 2014). The shifts in emphasis we have described are still too tentative to enable the German economy to give a powerful impetus to help overcome the euro zone crisis.

However, it is important not to overlook the paradox of development: the fact that private household demand since 2008 has been able generally to play a stabilising role, in contrast to before the crisis, is largely due to the overall more favourable development of wages. Because of the crisis and the broad public criticism to which it has given rise of the increasing social inequality in Germany the trade unions are in a somewhat better position with regard to wage policy. The positive effects thus triggered may in future be enhanced by the new labour market regulations introduced by the new German government (notwithstanding the relevant reservations: at least the further downward wage drift should be halted). However, precisely that which has helped Germany has dictatorially been refused to the crisis countries.

The paradox of development since 2008 can be summed up as follows: *the comparatively positive economic development is not to be attributed to 'Agenda 2010', but rather to the first attempts at limiting the*

damage caused by the Agenda 'reforms'. The growing trade union influence over wage development has played an important role here.

A bitter irony follows from this: the shift of emphasis, which caused a break in the uninterrupted continuation of the Agenda policy, not only makes it easier for German policy to make it appear at home that the cuts in government spending are, for the time being, less of a priority than elsewhere, but also – and this is perhaps their most important effect – it favours the presentation of Germany both at home and abroad as a model for Europe, justifying the German government's leading role in the implementation of the EU's fiscal dictatorship. The image of potentially the biggest victim of other countries' lack of budgetary discipline that the German government takes advantage of at the same time consolidates the domestic political base. This is a 'trick' likely to send any spin doctor into rapture, but it is fraught with pitfalls. The bogus labelling can continue yet awhile. However, a policy that, while tactically flexible, still adheres unswervingly to neoliberalism will get caught up in its contradictions.

3. Outlook: shifting coordinates

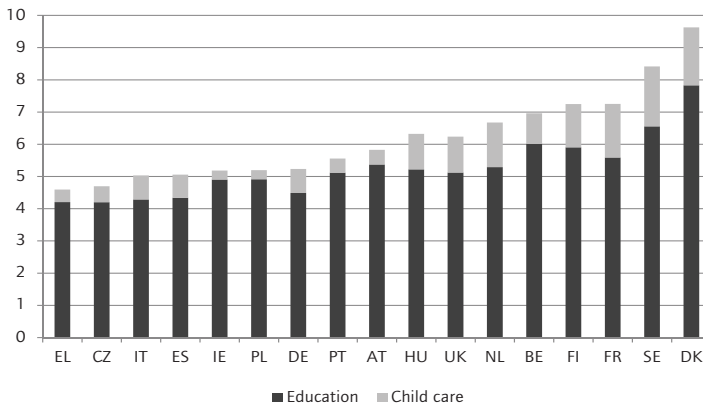
The limits of German economic policy to date are not initially discernible where it has been criticised most sharply, especially abroad, namely its export dependency. It may be that its unsustainability has been made more evident to a broader public in Germany due to the consequences of the so-called 'debt brake' and 'fiscal compact'. There is a lot to be said for the assumption that in the short and medium term, given increasing private wealth, public poverty in Germany will increasingly come to be regarded as unacceptable. Thus the proportion of public investment in GDP, which in any case is far below the EU average, had fallen to its lowest ever level by 2007, at 1.4 per cent, to which it returned after rising slightly up to 2012. Because the bulk of gross investment consists of replacement investment, net public investment since 2003 has been negative, in contrast to more than 2 per cent in 1980 and current comparable values of at least 1 per cent in the United States and France (Priewe and Rietzler 2010). The export world champions are thus preparing to meet the challenges of the future with a shrinking public capital stock.

Over half of public investment is carried out by municipalities, where the woeful state of public finances is most evident. According to a survey by

the German Institute of Urban Affairs (DIFU) cities and municipalities estimate their investment gap at around 100 billion euros (KfW 2012). The statistics on public investment include ‘only’ capital investments, not investment in *people*. However, the future development of the potential of the German economy and society depends on a viable education and training system and also all the social services that make it possible for qualified women to participate in the labour market. Germany is to be found in the lower midrange in the EU with regard to spending on such labour-intensive services. This becomes particularly clear from the OECD’s comparison of the proportion of public spending devoted to education and training, as well as child care, which amounts to 5.2 per cent in Germany in comparison with 9.6 per cent in Denmark and 7.3 per cent in France.

The German government and the great majority of the Bundestag have severely encumbered themselves with the ‘debt brake’ and played a decisive role in bringing it about that an even narrower constitutional limit was imposed on public debt across the EU. Lest we forget that all this was really done deliberately Olaf Scholz, SPD mayor of Hamburg and former minister in the federal government, in an interview with FAZ (27.2.2012)

Figure 7 Public spending on education/training and on child care as a proportion of GDP, selected EU countries, 2007



Source: OECD (2011).

declared that: 'No one really understands yet what a dramatic paradigm change we made with the debt brake. The much heralded "lean state" will come about of its own accord.' There is much evidence to suggest that turning away from this policy approach will require even more of a struggle than the one that made possible the recent tentative efforts to mitigate the damage caused on the labour market by Agenda 2010.

Germany's economy and society have the potential to play a positive role in Europe. But this will be possible only in conjunction with fundamental reform – in the true meaning of the word – of the German employment model. Particularly important elements of such reform would be:

- A boost for public investment and services in conjunction with a gender-policy modernisation of the welfare state and consistent progress with the new energy policy (the so-called '*Energiewende*') (DIW 2013). Such a restructuring would trigger a positive sum game with growth and self-financing effects and at the same time help both the economy and society to meet the challenges of demographic change.
- A substantial increase in taxes on profits, higher incomes and, in particular, capital (Schratzstaller 2011), without which such a change of course simply won't be possible. A little noticed aspect of such a tax reform would be to strengthen the social compensation mechanisms that, as already mentioned, are a tacit condition of the proper functioning of the 'wage formula' on which the industrial trade unions base their collective bargaining policy.
- Support for the weakened collective bargaining system not only by means of a statutory minimum wage, but also – just as important – by a fresh approach to declaring collective agreements generally binding, as well as equal pay for temporary work and making the awarding of public contracts conditional on adherence to (generally binding) collective agreements (Schulten and Bispinck 2013; Weinkopf and Vanselow 2008).
- Re-regulation of the labour market by an 'extension of the scope of protection of unemployment insurance'; linking the notion of 'reasonable' employment conditions to be accepted by job seekers to the criterion of payment of collectively agreed or customary local wages; the re-regulation of fixed-term employment, temporary employment and employment contracts; and the abolition of special regulations for mini-jobs (Bäcker *et al.* 2011; Bosch 2012).

This short overview already shows that, despite the first steps in the right direction taken by the present government, the bulk of a social reform of the German employment model will be the object of future political debate. This debate will be decisive for Europe: more social balance in the biggest European economy would reduce the constant pressure to lower wages and to dismantle the welfare state on the other countries in the region and in particular in the monetary union. Germany could become the engine of a socially and environmentally more sustainable reorientation of the EU. German industry would be in a position to develop its strengths in the area of environmental renewal, but besides economic incentives strong regulations are needed (especially with regard to the *Energiewende*) to encourage it to take on such a pioneering role. This policy can count on comparatively broad agreement in German society with regard to more sustainable use of natural resources. Even in the short term it would be possible to use a portion of the current account surplus and the fiscal crisis dividend for anti-cyclical government spending – that is, public investments in Germany and other EU countries – by means of which the strongest European economy could pull other parts of Europe along with it as an economic engine (Troost and Paus 2013). This would also represent a major gain in terms of democracy in the EU and its member states.

But this is a hope for the future. In the meantime, the German government is dictating a ‘reform programme’ based on cuts in social services to other countries with the authority gained by having already gone through it itself or at least – in the case of the ‘debt brake’ – by having introduced it and, as a result, doing better than everyone else. All this is based on a grand illusion: the mistaken belief that by expanding the alleged virtues of German stability it will be possible to continue to pursue the original business model of German capitalism in the euro zone. The interests behind this policy are powerful, but its prospects of success are weak.

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Conversion through inequality: the transformation of the French social model

Florence Jany-Catrice and Michel Lallement

After The economic crisis at the end of the 2000s cost the French economy dear. The number of people employed in the private sector – not including agriculture – fell by 187,000 between the start of 2008 and the end of 2009. Never in the past 40 years had job losses been so high and the situation has not improved in the meantime. However, this crisis is not confined to a loss of jobs or a decline and continuing weakness in economic growth. It is also rooted partly in economic and social inequality, while French policy in response to the crisis has only exacerbated this inequality. The outcome is the crumbling of the basis of the welfare state and, generally, of the French model.

In order to show this we shall first look at how this model developed before the crisis. Secondly, we shall examine how France has responded to the crisis, especially with regard to the labour market. Finally, we shall attempt, more than five years after the onset of the crisis, to identify what it has to teach us and to describe the consequences. The upshot is that France must find the strength to bid farewell to a number of economic dogmas.

1. The transformation of the French model before the crisis

France was no more immune to the neoliberal wave of the 1990s and 2000s than other Western countries. The country long had the reputation of maintaining so-called ‘Jacobin’ or ‘statist’ traditions, but today it looks very different from how it was at the end of the twentieth century. From a state-controlled capitalism a state-promoted capitalism has emerged (Berrebi-Hoffmann 2009). A number of factors have contributed to this transformation.

The first factor involves turning away from a system of company financing based largely on banks. In the 1970s 92 per cent of all investments were financed by banks. In 1994 bank loans still represented 55 per cent of the financial resources available to economic actors (besides resort to the financial markets and self-financing). Between 2000 and just before the onset of the crisis in 2007 the figure had fallen to 40 per cent. France has become one of the most financialised countries in the world, ranking just below tax and regulatory havens Luxembourg, Ireland and the United Kingdom. Before the crisis the value of the securities traded on the financial markets in France grew less rapidly than in the English-speaking countries, but the growth rate was striking nevertheless: in 2000 market capitalisation made up 112.7 per cent of French GDP, but by 2006 this had risen to 149 per cent. A series of developments contributed directly to this trend: the emergence of so-called 'financial innovations', securitisations (an instrument with whose help non-liquid assets can be traded on the market) and the increasingly important role played by institutional investors, such as investment companies, pension funds and insurance companies. As a consequence of this financialisation the stock exchange has relentlessly gained ground at the expense of the real economy. On top of that, borrowers are in a less happy situation than previously because the financial system has made loan arrangements more tenuous. The financial markets have thus come to play a more important role in the French economy.

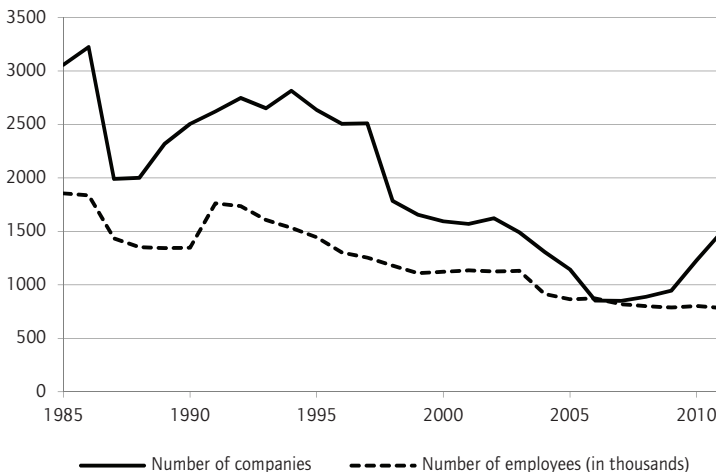
Meshing with these changes in the financial system the upheavals in the production system constitute the second aspect of the current transformation of the French economy. In the 1990s an extensive concentration of capital and enterprises took place, manifested in mergers and takeovers in numerous sectors. Under the aegis of a focus on core business, cost cutting and cultivation of economies of scale were deployed to step up the profitability of capital investments. Against the background of wage moderation the merger strategy – which bombed spectacularly in many instances – aggravated the fault lines in the labour market. Above all, the phalanx of employees in poverty, who are not in a position to maintain subsistence with their wages alone, point to the growing significance of a 'precariat' among French wage-earners (Castel 2003). The French trade union movement, as divided as ever and continuing to suffer from low membership, was as poorly prepared as many others to address this problem. Collective bargaining had been decentralised and much more than in the past flexibility with regard to employment and working conditions became a bargaining chip, which did not make it any easier to organise broad-based social protest. Sometimes these protests were instigated by

a new breed of civil society networks, such as the farmers' association or tenant movements. These groups normally act alongside traditional trade unions and not in cahoots with them.

Thirdly, the French model has long benefited from a large proportion of public companies, but here too there were massive upheavals: since 1987, in various privatisation waves – even by left-wing governments – the number of firms with a majority state holding was reduced by around half (Figure 1).

Furthermore, since the late 1980s many 'reforms' had been introduced with the declared aim of reducing the debts of public companies and increasing the 'efficiency' of public spending, which often amounted to the withdrawal of the state and job cuts in the public sector. Other aims included closer control of such companies, internal restructuring (such as the establishment of independent company managements), the switching of certain tasks to the responsibility of municipal authorities and the simplification and improvement of relations between the citizenry and the administration (for example, based on the principle of 'everything under one roof'). Expenditure ceilings and the so-called 'asymmetric transferability rule', in accordance with which items of staff expenditure

Figure 1 Number of firms with a majority state holding, 1985–2011



Source: INSEE.

can be used for other purposes, while the reverse is not permitted, options for public sector job creation were narrowed. Although these measures were in part introduced before the economic crisis of 2007/2008 their effects were aggravated by the measures taken to combat it.

2. The response to the crisis since 2008

In 2008 France's macroeconomic indicators turned to red – just like everywhere else. According to the Institut national de la statistique et des études économiques (INSEE) GDP fell by 2.7 per cent between 2007 and 2009 (against an EU average of 3.2); investment fell by 8 per cent, imports by 8 per cent and exports by almost 11 per cent (Table 1). The unemployment rate rose by 3 percentage points during the same period.

Table 1 Changes in GDP and its components (%)

	2006	2007	2008	2009	2010	2011	2012	2013
GDP	2.5	2.4	-0.2	-2.9	2.0	2.1	0.3	0.3
Imports	5.1	5.7	1.3	-9.4	8.9	6.3	-1.7	1.7
Gross fixed capital formation (investment)	4.0	5.5	0.9	-9.1	2.1	2.1	0.3	1.0
Exports	5.2	2.8	0.4	-11.3	9.0	6.9	1.1	2.2

Source: National Accounts – Basis 2005, INSEE.

However, France was not among the countries hit hardest by the crisis. In fact, in comparison with the previous recession in the early 1990s, the country appeared to be holding up better, at least as regards jobs. While in 1992/1993 value creation in the private sector (not including agriculture) fell by 1.9 per cent and employment by 2.1 per cent, the fall in employment in 2008/2009, despite a collapse in GDP of 5.3 per cent, was 'only' 2.5 per cent. The labour market thus did not shrink so dramatically in comparison with the economy as in the early 1990s.

There are several reasons for this development. In contrast to Germany wages had largely kept pace with productivity in the preceding years, so that the domestic market had maintained its comparative significance for economic growth, which continued during the crisis (Table 2).

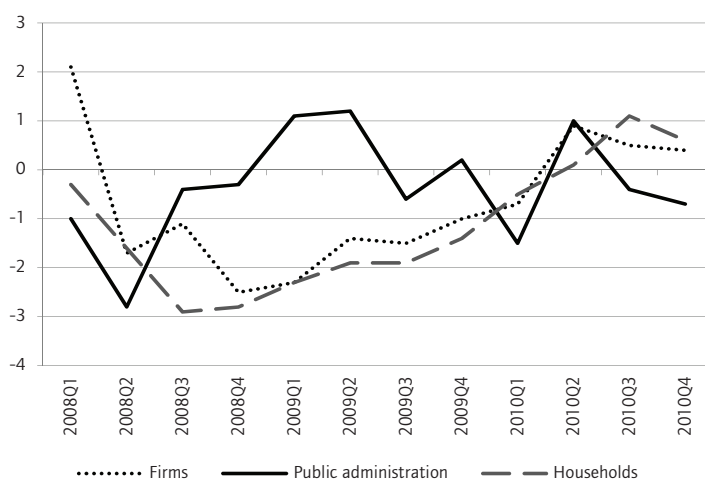
Table 2 Germany and France compared: development of selected indicators (average annual growth rates, adjusted for prices)

	GDP		Private consumption		Government consumption		Gross fixed capital formation		Exports		Imports	
	DE	FR	DE	FR	DE	FR	DE	FR	DE	FR	DE	FR
1999–2007	1.7	2.2	0.9	2.7	0.8	1.6	1.2	4.1	7.8	3.8	6.0	5.6
2008	1.3	0.4	0.4	1.0	2.1	1.2	3.1	0.6	2.9	–0.2	4.3	0.8
2009	–5.0	–2.2	0.2	0.8	3.0	1.5	–8.9	–6.2	–14.2	–10.9	–8.9	–9.5

Source: Horn *et al.* (2010) (Eurostat).

On top of this came the relatively high household savings rate (around 15 per cent), which also prevented a collapse in consumption during the economic crisis. Another important factor, which explains the relative stability of the French economy during this period, was state investments (Figure 2). These short-term developments were part of a struc-

Figure 2 Development of private and public investment, France, 2008–2010 (%)



Source: INSEE.

tural trend that enabled France to fare better than eternal rival Germany with regard to economic growth, investments and consumption since the 1990s (Horn *et al.* 2010). Its more sustainable – in comparison with Germany – domestic demand enabled France to make up for weaker exports and thus to weather the global recession more successfully. This support from the public sector formed part of a recovery plan in the amount of 34 billion euros for 2009 and 2010. Even though the plan has not met all expectations it has undoubtedly helped to limit the number of bankruptcies and to improve companies' liquidity. However, it once more revealed the inclination of the Sarkozy government to put the interests of companies above those of employees.

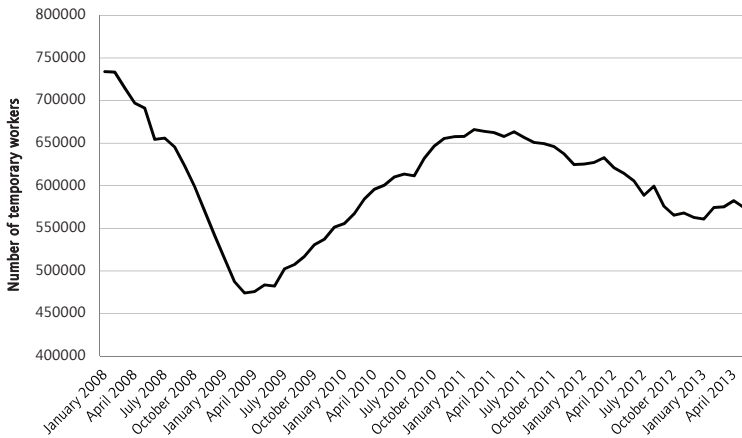
Companies reacted largely along the same lines as during previous crises (Liégey 2009). In accordance with the logic of internal labour markets large French companies began to protect their skilled employees by means of short-time working.¹ In this crisis this instrument was utilised much more than in earlier recessions. The number of employees with regard to whom short-time working was authorised had fallen by 82 per cent between 1996 and 2005, that is, from 1.7 million to 300,000 (Calavrezo *et al.* 2009). In 2008, however, the scheme was revised, enabling companies to extend working time reductions imposed on employees over a longer period. The economic crisis accelerated resort to this new device. Thus, for example, in the first quarter of 2009 more than 10 per cent of employees in the automotive industry were put on short-time working (Conseil d'analyse stratégique 2009).

French companies passed on the costs of the crisis to their least secure employees. In a little over a year the number of temporary employees fell by a third. A similar strategy could be observed in 2012 when after a brief recovery the economy cooled once again. As if we need to be reminded, the data show how important temporary employment is as an instrument of flexibility (Figure 3).

While the collapse in temporary work in 2009 occurred largely in industry the service sector reduced employment by cutting fixed-time working. Other instruments – such as reducing overtime, collective holidays and further training measures – were deployed only to a limited extent. Working hours were varied only slightly during the crisis. The flexibili-

1. By contrast, small companies scarcely used this option, which explains another difference with Germany, which resorted to such arrangements on a much larger scale.

Figure 3 Development of temporary work in France, 2008–2013



Source: Pôle emploi.

sation measures that had been agreed in the course of introducing the 35-hour week at the end of the 1990s, the early 2000s and subsequently were not therefore used to counteract the effects of the crisis.

Overall, in the short term French companies resorted primarily to internal flexibility, as they had always done in previous decades. In the medium term, however, external flexibility has gained ground. The background to that is not only that 14 per cent of dependent employees in France are in precarious employment – fixed-term, temporary, internship – but protection of employees by means of permanent contracts has receded. The crisis was both a shock and a pretext for reducing the importance of internal workforce flexibility in favour of external flexibility and for increasing inequality between employees (for example, between permanent well qualified white-collar employees or skilled workers in the public sector, on one hand, and precarious employees on the other). The French state can scarcely offer an example for companies to follow in this instance: in 2008, 873,000 workplaces in various public institutions – administration, hospitals, local authorities – making up 16.5 per cent of all workplaces in the public service, were occupied by precarious employees, in contrast to 664,000 in 1998.

The mainly cyclical adjustments conceal a difficult structural situation, both economically and socially. Up to 2013 the unemployment rate per-

sisted at a high 10 per cent, with long-term unemployment reaching 3.7 per cent (according to INSEE). This had last been observed in the early 1990s. The consolidation of high unemployment retards wage growth and weakens effective demand; in other words, the very factors that had stabilised the French economy in the years leading up to the crisis.

There is another element that has helped to stymie economic recovery since the shock of 2008: the rise in public debt. As in other European countries the French government has imposed a restrictive budgetary policy, which has acted as a stumbling block for a demand-driven upturn. Even François Hollande did not deviate from this after coming to power. Box 1 provides an overview of the main labour market and social policy measures.

Box 1 The French government's main labour market and social policy measures since 2012

Youth unemployment

Jobs for the future: The law creating 150,000 'jobs for the future' was one of the first measures adopted by the Hollande presidency. Support is to be given to young people, especially from deprived areas, by making available full-time jobs for a maximum of five years. The jobs are paid at the minimum wage (SMIC) and financed up to 75 per cent by the state. The remaining 25 per cent has to be found by the municipal authorities, associations, foundations or companies that provide the jobs.

Intergenerational contracts: the idea is to stimulate company schemes by means of state support in which older employees – 55 years of age or over – show new permanent young employees (below 30 years of age) the ropes and mentor them. The companies concerned will be exempt from all social security contributions for the young employees and from the employer's contribution to unemployment insurance for the older employees for five years. The target is to introduce up to 500,000 such contracts, but according to initial estimates (taking into account deadweight effects) 100,000 additional jobs are to be anticipated (OFCE 2012).

Pension reforms

Pension reforms represent a radical shift in the social security system. Hollande's policy does not deviate from that of his predecessor. First of all, retirement two years early was made possible for those entering the labour market below 20 years of age. At the same time, a heated public debate commenced on the financial sustainability of the pension system. Against the background of more

recent analyses by the European Commission, however, some economists have pointed out that, given France's demographic development, its pension system faces fewer problems than, for example, Germany's, although the statutory retirement age in France is substantially lower (Cornilleau/ Sterdyniak 2012). They also point out that because of France's more dynamic demographic development its public debt will be more sustainable in the long term than that of Germany. Thus it is also crucial for the funding of the pension system to sort out family policy (financial assistance, expanding public child care provision and expanding care services in general).

Housing policy

The housing act of 2013 is intended to halt rent increases in 38 large cities in France, which in recent years have exerted considerable downward pressure on living standards, especially in the poorest households.

'Flexicurity'

In early 2013 the peak organisations of the employers and three trade union federations (CFDT, CFE-CGC and CFTC – CGT refused to sign) signed a 'national framework agreement on flexicurity', which was then adopted into law (Lallement 2013). It extends the options for reaching agreement at enterprise level on securing employment in exchange for wage cuts or working time measures and, at the same time, makes it easier to lay off workers for economic reasons on the basis of enterprise agreements. Although it gives employees some new guarantees, to date there is no evidence that this arrangement could form the basis for a new model that would be both economically efficient and socially just.

The 'responsibility and solidarity pact'

At the beginning of 2014 President Hollande proposed a pact whose basic idea he summarised as follows: 'lower taxes and other levies on labour, lower impediments on entrepreneurial activities in exchange for more new hires and more social dialogue'. The aim is to simplify bureaucratic procedures and to reduce labour costs by means of a 'tax credit for competitiveness and employment' (CICE), as well as other tax concessions for companies. At the same time, the net wages of low income employees (less than 1,500 euros net per month) will be raised by reducing social contributions; employees on less than 1,250 euros shall also receive additional tax concessions and social benefits for those in poverty will be improved. This pact is controversial, being framed in terms of liberal supply-side economics. Particular criticisms have accrued to the fact that it remains unclear what evidence will be accepted for the retention or creation of jobs, in return for which companies will enjoy lower labour costs, as well as the fact that the pact will be paid for by further cuts in public spending.

3. Interim results and future prospects

How do things stand more than five years after the crisis of 2008? At this point we cannot give an exhaustive answer, but we take the view that the French model has not emerged from the recent economic upheavals unscathed. This can be seen in terms of three problems that concern the core of the model and each of which represents a major challenge.

Productivity development and competitiveness

A first consequence of the crisis concerns productivity development. Per capita labour productivity fell between the 1980s and the early 1990s, but by 2007 it had risen again (Berrebi *et al.* 2009). The ensuing collapse in productivity in 2008 was scarcely surprising as a consequence of measures to safeguard employment implemented in the midst of a deep recession. Many economists, however, have diagnosed an attenuation of longer term trends in productivity growth. According to this view, tertiarisation explains more than half the weaker productivity growth trend since the 1990s. However, since the early 2000s productivity development has also slowed down in other sectors, including industry (Argouarc'h *et al.* 2010; Schreiber/Vicard 2011). The current crisis has thus brought to the surface deeper lying structural problems. Thus – according to Eurostat figures – the share of manufacturing in France's GDP fell from 15 per cent to 10 per cent between 2000 and 2010, while in Germany it remains between 22 per cent and 23 per cent.

Competitiveness plays a key role in the public debate on this problem. Although competitiveness is often taken to be an indicator of the health of an economy, this applies – if at all – only to sectors exposed to international competition. In particular, however, it is frequently overlooked that competitiveness can be due both to favourable cost and price development by international comparison (with regard to which the development of costs and prices in turn determines profits) and to the superior quality of the product, which is of course difficult to measure. Furthermore, there is no systematic connection between competitiveness and growth. If, for example, price competitiveness is largely achieved by means of wage cuts and not by improving productivity this will be counterproductive in the medium term with regard to the economy and growth.

Critical economists point to a fundamental lack of innovation on the part of French industry, as evidenced by a lack of products whose sales do not depend primarily on price developments. A significant indicator in this context is the fact that in French companies an increasing proportion of net profits is being distributed to the shareholders. If one compares this with spending on research and development a dismaying picture emerges: in 1992 research and development spending in corporations amounted to 45 per cent of dividends; by 2011 this had plummeted to around 25 per cent (Coutrot *et al.* 2012).

The debate in France, however, remains focused on price competitiveness. Recent reports commissioned by the French government – in particular the Attali report – show how much neoliberal dogma on labour cost reduction has sidelined the issue of competitiveness based on quality. This should be borne in mind when considering the following data. According to the IMF, French exports in 2011 made up 3.5 per cent of world trade in comparison with Germany's 8.2 per cent. In France these exports made up 29 per cent of GDP. In the French public debate this is linked to the unfavourable development of unit wage costs in comparison with those of Germany (on this see chapter on Germany in this volume). This gives impetus to political demands to emulate the policies of Schröder and Merkel. Apart from the fact that the gap between the two countries in terms of unit wage costs has not widened in the past five years, one must question a logic fraught with so many dangers (such as wage cuts and threats to health and the environment). It would be better to pursue new economic development strategies that 'break with destructive consumerism' (Coutrot *et al.* 2012) and are directed towards environmental transformation, social services and reducing social inequality (Coutrot/Gadrey 2012). Germane to this purpose would be utilisation and reinforcement of existing potential in terms of regional economic cooperation, especially small and medium-sized companies.²

2. So-called Pôles Territorial de Coopération Economique (PTCE) ('Territorial hubs of economic cooperation') could serve as a model for this, in which small and medium-sized companies, local authorities, research and training institutions and other networks develop joint initiatives and innovations to promote sustainable economic development in a region.

Territorial and social inequality

Up to the 1980s in France a strong government, enjoying high tax revenues, was regarded as part of a 'Jacobin' and social tradition that the state claimed as its own. In the course of the past decade, however, along with a fall in tax revenues (in relation to GDP) decentralisation has been implemented as a result of which competences, especially with regard to social security and education, have been transferred to the regions and the Départements (Aurissergues 2010; Champsaur and Cotis 2010).

While decentralisation is based on the logic of territorial proximity – dealing with local situations in terms of local needs – and subsidiarity it has also heightened territorial inequalities of access to public services, a new development in the French tradition of equal rights. It is becoming increasingly clear that there are substantial differences between the French regions. For example, although the region of Nord-Pas de Calais has had some partial successes with regard to structural change and has been able to heal many of the scars of nineteenth-century industrialisation, it suffers from a high level of poverty. Regional GDP is just over half the average for the Ile de France region; the proportion of people without qualifications (beyond the school leaving certificate) is 36 per cent, which is 10 percentage points higher than in the Ile de France; and life expectancy is four years lower.

Territorial and social inequality are closely intertwined. Since 2008 income inequality has become a permanent issue in French politics. This may surprise some because inequality rose only slightly in France between the mid-1990s and the eve of the crisis or – depending on how it is measured – even fell slightly (ONPES 2010). However, the biggest inequalities are to be found at the two ends of the income and wealth spectrum. In fact, before the crisis the income growth of the richest households in France was spectacular; according to INSEE, the annual income of the richest 0.01 per cent of the population rose by 40 per cent in only three years (2004–2007), in contrast to a 6 per cent increase among the poorest decile. The crisis has exacerbated this inequality: according to Eurostat, the poorest 5 per cent of French households have lost 0.3 per cent of their nominal average income, while the richest percentile have gained 9.7 per cent.

Wealth inequality is even more striking. In 2003 the highest decile owned almost half of all the wealth in France. Due to various tax con-

cessions on wealth (with regard to inheritance and wealth taxation, as well as capital gains) ‘inheritance capitalism’ was consolidated (Philippon 2007). These tax concessions are emblematic of a policy ‘catering for rich people’, but contributed to imbalances in the public budget and reduced the scope for social measures needed to help the poorest.

Poverty: the crisis and a new social problem

As a result of the economic crisis rising poverty, the working poor and the economic policy that is responsible for such rents in the social fabric have become the centre of attention. The crisis is not the sole cause of precarity and poverty, but it has exacerbated the problems.

As already mentioned the crisis was not the only reason for rising unemployment, but it did extend its scope. For example, in spring 2013, according to the estimates of the research department of the labour ministry (DARES), there were 3.2 million unemployed in category A (people without a job, but actively looking for one), but taking into account various forms of underemployment, as well as labour market policy measures, the figure was closer to 4.7 million. The proportion of people in involuntary part-time work alone was estimated at 5 per cent (INSEE). The rise in unemployment is concentrated in certain population groups, such as young people, whose unemployment rate rose by a quarter between 2008 and 2010 and by 2013 had reached more than 25 per cent (young people available for work). Against this background the economic crisis exacerbated the trend towards a weakening of regular employment: in 2010 almost 80 per cent of all new hires were on the basis of atypical contracts.

All in all, these developments could lead to an increase in the number of working poor, a notion and a social reality that are still very new to France, in contrast to the United States. Based on a threshold of 60 per cent of average income the number of employees on low wages rose from around 150,000 in 2003 to 1.925 million in 2010. The self-employed are overrepresented in this category and one-fifth of the working poor are part-time employees (OPNES 2010).

Hitherto, poverty in France has primarily affected jobless people living alone. In 2008 there were around 8 million people in households with incomes below 60 per cent of the average. However, without the social security net this would be 25 per cent of all households. This difference

between poverty before and after transfers ranks France alongside Sweden among countries with the most robust protection mechanisms.

This social system undoubtedly did much to counteract the economic crisis of 2008. However, two caveats apply given how things have developed in the meantime. First, the priority with regard to employment policy is workfare, as in the English-speaking countries, so that as social benefits and services are scaled back the number of working poor is likely to increase (Ponthieux 2009). Secondly, young people below 25 years of age are not only harder hit by unemployment, but also less protected against possible income cuts. The reason for this is that government social protection programmes are much less generous for young people (Zemmour 2010).

Finally, it is important to note that the problem of poverty cannot be addressed adequately without taking gender into consideration. There are two reasons for that: first, active labour market policy measures can confer the status of occupation on some typically female activities – such as ancillary work in day nurseries, the household or in care – in order to make them worthy of support. Such activities, generally carried out in the household or in social organisations are characterised by low income and poor working conditions. Secondly, part-time work is the main cause of low monthly wages. Because the female share in part-time working is 82 per cent it is not surprising that 75 per cent of employees in the low wage segment are women.

Summary

The economic crisis of 2008 cannot be regarded as a random event in France any more than anywhere else. The crisis took various forms depending on the national economic and social model, but it gave rise to upheavals in current capitalism, in the first instance arising from the financialisation of the economy. For a number of reasons, which we have elucidated in this chapter, France fared better in the crisis than other countries, at least in the short term. From this perspective the strategy of immediate government intervention – long a feature of the French model (Berrebi *et al.* 2009) – can explain positive developments in France, by European comparison. However, the French government no longer plays the role familiar from 20 years ago, and its policy of public sector ‘modernisation’ has given the helm over to new actors from the public and the private sector, who approach employment issues from a differ-

ent – sometimes less favourable – perspective. However, the capacity to implement centralised plans in order to combat an economic downturn has not been lost; even if that does not involve conducting proper negotiations with political and social actors. The crisis of 2008 provides considerable evidence of that, but at the same time it revealed and accelerated some fundamental changes, in particular social inequality, which we have looked at.

The structural trend towards more inequality and poverty testifies to the transformation of the French model. Social solidarity has gradually crumbled due to various reforms over the past three decades. The increase in the number of working poor has brought to light a new social problem. Ultimately, the crisis, by exacerbating inequality and acting as a pretext for further neoliberal social adjustments, has served to justify this medium-term development. Thus despite the satisfaction with the fact that France fared pretty well, at least in the short term, after the economic shock in 2008 there is every reason not to be particularly optimistic with regard to the next few years.

This is also indicated by the various measures implemented in response to the crisis in the euro zone. They have confirmed and reinforced the liberal orientation pursued by economic policy in France for many years now. This also applies to the abovementioned ‘National Framework for Flexicurity’. The basic weakness of all these arrangements is that they are based on the idea that unemployment is ultimately due to a lack of labour market flexibility.

The French economy is in crisis, but what we are seeing is primarily a crisis of the ‘software’ of the economy and economics, which refuse to recognise the crisis’s structural bases: inequality (and thus the constriction of aggregate demand) and the destruction of natural resources.

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Mastering the crisis but not the future: the Austrian model in the financial and economic crisis

Christoph Hermann and Jörg Flecker

1. Dynamics of the Austrian model

The *Wall Street Journal*, writing about Austria in 2006, noted that the once sleepy, corporatist economy had changed into one of Europe's most competitive thanks to 'free-market reform' and tax cuts. Perhaps this is an exaggeration. Austria still has significant corporatist institutions and the liberalisation of markets has not gone as far as hoped for by the country's economic elites, especially in the area of public services. However, there is no doubt that the Austrian model has undergone far-reaching changes since the mid-1980s, when an economic crisis put an end to the post-war system (Hermann and Flecker 2009).

While in the post-war decades Austria had a high share of public ownership in industries and banks and extensive market regulation that sheltered businesses from international competition, much of what has happened during the past three decades has been intended to create an environment that is attractive to foreign capital and to make native capital more competitive. Subsequent measures have included the liberalisation of trade and capital flows and the reduction of corporate taxes. Lower tax revenues, however, have aggravated budgetary problems and demands for budgetary austerity and cuts in the welfare system. As a result, economic and social policies have increasingly been subordinated to the overall objective of improving corporate profitability.

Many of the changes were facilitated through Austria's accession to the EU in the mid-1990s, which in turn led to a further Europeanisation and internationalisation of the Austrian economy. While the liberalisation of the economy was accompanied by significant job losses in certain sectors – such as the electronics and chemical industries – due to the concentration and relocation strategies of international firms, Austrian

capital has profited immensely from the EU's eastward enlargement. Austria has profited in particular from the introduction of the euro, which ultimately helped the country to move from a current account deficit to a surplus, with surpluses based mainly on gains in trade in services, including banking and retail activities. But while profitability and productivity soared along with internationalisation and the growing shareholder-value orientation, unemployment has remained high compared with the post-war decades (but low compared with other EU member states).

In terms of economic policy Austria has come much closer to what one might call the neoliberal mainstream. Two aspects of the Austrian reform process are particularly interesting: the transformation took place slowly, developing over several decades – the first 'austerity package' was introduced in 1987, while the last major welfare cuts took place in 2003. The changes were partly masked by institutional continuity (Hermann and Flecker 2009). Apart from a brief period of right-wing government (2000–2006) the social partners continued to play a substantial role in mitigating policy differences, even though the outcomes were generally more beneficial to capital than to labour. As a result, the changes took place without major resistance from organised labour. On the contrary, the trade union movement defended most of the austerity packages (except those adopted between 2000 and 2006) and Austria's accession to the EU.

Another feature with regard to which Austria has shown remarkable stability is the 'conservative welfare state', with its high proportion of cash-based benefits. Despite some attempts to improve the situation of women, welfare institutions continue, in effect, to discriminate against women and other individuals with low incomes and discontinuous working careers. As a result, social inequalities have tended to increase despite a comparatively well developed welfare state and a stable and comprehensive collective bargaining system.

Inequalities are fuelled partly by the transformation of labour markets (Atzmüller 2009). Even though Austria has not experienced a direct attack on employment standards and security, atypical and sometimes precarious forms of employment have emerged alongside the standard employment relationship. By far the most important form of atypical employment is women working part-time hours. The employment rate of women has increased, but it is still far below that of the Nordic countries, especially if counted in full-time equivalents (Mairhuber 2010).

Three aspects of the transformation of the Austrian model have made the country particularly susceptible to the effects of the crisis: first of all, with economic liberalisation Austria has become more closely integrated in the European and world economies, while very moderate real wage growth and austerity policies have made it even more dependent on exports and hence on external demand. Secondly, privatisation spurred the transformation of the banking sector from a public utility into profit-maximising businesses, which are eager to take major risks if they promise extraordinary returns. EU enlargement into central and eastern Europe encouraged Austrian banks to turn themselves into international financial institutions with major branches in the new member states. The banking sector grew, with the effect that assets account for over three-and-a-half times of GDP (IMF 2013). For years these investments generated extraordinary returns but they have turned out to be a major liability during the crisis, which has hit countries such as Hungary, Bulgaria and Romania particular hard. Thirdly, low real wage growth and a persistent fall in the wage share (wages as a proportion of GDP) have not only limited internal demand but have also contributed to the trade imbalances within the European Union, aggravating the crisis for a number of peripheral member states and ultimately threatening the European integration project.

2. The crisis in Austria

The crisis hit Austria in the second half of 2008, ending a phase of accelerated growth that had started in 2003. GDP growth rates reached 3.5 per cent annually in 2006 and 2007, fuelling profits and inflation. After years of stagnation, workers also capitalised on the favourable economic climate and achieved significant real wage increases in 2006 and 2007. Growth also resulted in a fall in the unemployment rate below 4 per cent (Labour Force Survey) just before the crisis struck in 2008. GDP growth fell in the last quarter of 2008, but overall GDP still grew by 2 per cent in 2008 (Scheiblecker *et al.* 2010: 322). The situation changed in 2009. In the first quarter of 2009 the economy contracted by 2.2 per cent compared with the fourth quarter of 2008 and by 4.9 per cent compared with the first quarter of 2008. The economy continued to shrink until mid-2009 with the effect that GDP fell by 3.6 per cent annually. The last time the Austrian economy recorded such a decline in GDP was in 1949 (Scheiblecker *et al.* 2010: 323). Despite the massive blow the Austrian economy still performed better than many

other European economies, including Germany, where GDP fell by 5 per cent (*ibid.* 234).

The Austrian economy has always been highly dependent on exports, especially to its main trading partner, Germany. However, the internationalisation of the banking and other sectors has intensified relationships with other countries, including the new member states in central and eastern Europe (Hermann and Flecker 2009). The outbreak of the crisis and the following financial hysteria immediately affected the Austrian banking sector. The government quickly adopted a 100-billion-euro rescue package to calm investors and depositors. Nevertheless, total bank assets fell by 3.3 per cent in 2009 (Scheiblecker *et al.* 2010: 323).

Besides the banking sector the crisis has mainly affected exporters. Total exports fell by 20 per cent in 2009. Among the export sectors, manufacturing was hit particular hard and within the manufacturing sector the main victims were producers of investment and durable consumption goods and related intermediate products. Output in manufacturing started to fall in the fourth quarter of 2008. Some manufacturers struggled with a 30 to 50 per cent decline in orders (Hermann 2011).

With some delay, the crisis also affected the construction sector. Even though Austria experienced a marked growth in construction in the years leading up to the crisis, the boom was not comparable to the situation in Spain or Ireland and was definitely not the cause of the crisis. Output decreased by 7.6 per cent in the first quarter of 2009 and by 2.3 per cent annually (Scheiblecker *et al.* 2009: 372). The decline in private demand was partly offset by public investments. These investments spurred growth in the construction sector in the fourth quarter of 2010 (*ibid.*).

The economic crisis quickly turned into a labour market crisis, but the reduction in employment was less severe than the contraction in GDP. While GDP fell by 3.6 per cent in 2009, unemployment increased by 1.4 per cent (Scheiblecker *et al.* 2010: 361). The number of unemployed persons increased by 57,000 from June 2008 to June 2009, while the number of participants in training programmes rose by almost 16,000 over the same period (Stiglbauer 2010: 28). Following the trajectory of the crisis, job losses first appeared in the manufacturing sector, with losses in February 2009 outstripping employment gains for the first time in six years. Over the course of 2009, employment in manufacturing fell by 6 per cent (Scheiblecker *et al.* 2009: 369).

Unemployment increased quickly and at an increasing pace until June 2009, when 33 per cent more unemployed persons were registered than in the preceding month. Overall, unemployment increased by 48,100 persons or 22.6 per cent from 2008 to 2009. In terms of registered unemployment, the unemployment rate increased from 5.8 per cent in 2008 to 7.2 per cent in 2009 (*ibid.* 366). If people in training and other labour market service measures are included, unemployment reached 9.6 per cent in 2009 (*ibid.* 368). According to Eurostat, unemployment accounted for 4.8 per cent in 2009 and was therefore significantly lower than in most other European countries (*ibid.* 366).

Among the first workers who lost their jobs were temporary agency workers. The number of agency workers increased significantly during the economic boom preceding the crisis, but declined by 15.9 per cent between July 2008 and July 2009; in manufacturing the reduction amounted to 32.8 per cent over the same period (*ibid.* 365). Employment cuts in manufacturing and in employment agencies combined were as big as in the rest of the economy put together (Stiglbauer 2010: 28). However, agency workers were not only the first to be laid off. They were also the first to be re-hired after growth started to pick up again in the second half of 2009 (Allinger 2011).

3. Responses to the crisis

3.1 Fiscal policy

In the face of the crisis, Austria, like many other countries in Europe and around the world, temporarily returned to Keynesian deficit-spending. As a first measure the government adopted a 'generous' rescue package for the Austrian banks. The government pledged to inject up to 100 billion euros into the banking system, if needed. The rescue package was extremely large relative to the size of the country and reflected the enhanced exposure of Austrian banks in central and eastern Europe. Rescue measures included the partial nationalisation of three major banks and financial support for others.¹ Up to the end of 2010 the government spent 5.874 billion euros on buying up the shares of troubled banks and took over banking-sector liabilities in the amount of 23.215 billion euros (Bundesrechnungshof 2012).

1. Hypo-Alpe-Adria, Kommunalkredit and Volksbanken.

In addition to bailing out banks, the government also adopted two economic stimulus packages to help the struggling economy. The volume of the package was 12 billion euros, or 3.5 per cent of GDP (Breuss, Kaniovski and Schratzenstaller 2009; Berger *et al.* 2009). The main stimulus came from tax cuts for households and tax credits and subsidies for companies. A major tax reform which was initially planned for 2010 was brought forward and adopted in 2009. The tax giveaways accounted for 2.1 per cent of GDP, although they benefited mainly high earners. Households in the first four income deciles gained less than households in the tenth income decile (*ibid.* 36).

In terms of expenditure, stimulus money went mainly to the modernisation of railway infrastructure and road construction – not least to support the construction sector. Investments in social infrastructure included the introduction of a cost-free kindergarten year for children before they start school, but in sum they were fairly marginal. Instead, deficit-spending mainly followed the traditional spending path and barely promoted structural change, social innovation or ecological modernisation. On the contrary, the stimulus package also included a 22.5 million euro car scrappage premium to support the ailing auto (supplier) industry.

As a result of deficit-spending, the annual deficit increased from 0.9 per cent of GDP in 2008 to 4.1 per cent in 2009 and 4.6 per cent in 2010; the total deficit increased from 63.8 per cent of GDP in 2008 to 69.2 per cent in 2009 and 72.4 per cent in 2011. In order to tackle the growing deficit, the government adopted an austerity package in 2011, totalling 6.3 billion euros (Schratenstaller 2011 and 2013). Except for a special tax levied on banks in exchange for the support they received during the crisis, the major part of the additional revenues came from consumer taxes. This means that lower income households contributed a significantly higher proportion of their income to the fiscal consolidation than high income households. Low income households also suffered from cuts in welfare spending, including cuts in care benefits and family allowances. Overall, the cuts mainly affected those who are most vulnerable and thus aggravated rather than alleviated social problems.

3.2 Labour market policy

The government adopted a number of measures to tackle rising unemployment, pooled in two labour market packages. The most popular

measure was the reform of short-time working. The reform was based on a social partner agreement, underlining the role of the social partners in mitigating the effects of the crisis. Short-time working existed before the crisis but played only a minor role. Among other things it was used to help companies affected by environmental disasters, such as floods. In October 2008, just before the outbreak of the crisis, 400 workers were registered as taking part in short-time working schemes (BMASK 2010: 300). From the social-partner perspective, short-time working is particularly attractive because it helps companies to retain qualified staff and avoid lay-offs, while most of the costs are covered by the government (Hermann 2011).

The reform was based on two amendments of the existing regulations. The main improvements concerned an extension of the short-time working period, first to 18 and then to 24 months. At the same time, the proportion of short-time working was extended to any number of hours between 10 and 90 per cent of regular working time (BMASK 2010: 293–94). The reform also introduced a rebate for employer social security contributions after six months of short-time working and special financial incentives for companies that combine short-time working with training or further education (*ibid.*). Further details of the introduction of short-time working were regulated in an inter-sectoral framework agreement negotiated between the Chamber of Economy and the Trade Union Federation (Allinger and Flecker 2010; Hermann 2011). Austrian companies also need a company agreement signed by a works council and a trade union representative if they want to switch to short-time working.

The two main unions representing workers in the industrial sector (PROGE and GPA-DJP) agreed that they would sign company agreements only if the affected workers receive 90 per cent of their regular wages, regardless of how many hours they were working. Because about 60 per cent of wages was covered by the Labour Market Service (the rate for unemployment benefit), the rest had to be paid by the companies concerned. Except in a number of small and medium-sized companies the unions were mostly successful in obtaining the 90 per cent replacement rate. While the social partner negotiations on the short-time working reform ran fairly smoothly, introduction on the company level occasionally sparked conflicts (Hermann 2011).

Short-time working is widely considered a success. It was used mainly in automobile production and by auto suppliers, as well as in engineering and the

metal sector more generally. At the peak of development in April 2009, more than 300 companies had introduced short-time working, affecting more than 37,000 workers (BMASK 2010: 300). The Federal Ministry of Employment, Social Affairs and Consumer Protection estimates that short-time working saved approximately 30,000 jobs (BMASK 2010: 304). Alfred Stiglbauer (2010: 35), however, estimates that the employment effect was only 6,800 jobs or 0.2 per cent of total employment.

While short-time working is considered a success, combining short-time working and further education was largely a failure. Only 20 per cent of workers on short-time working used the opportunity to improve their skills (*ibid.*). One reason may be that the additional incentives were targeted towards companies instead of workers worried that their jobs would still be there after the crisis. Another reason is that qualifications typically need long-term planning, whereas the crisis required *ad hoc* action (Bock-Schappelwein, Mahringer and Rückert 2011). In any case, while some workers were reluctant to combine short-time working with further training, many took the opportunity to go on training leave paid by the Labour Market Service for up to 12 months on 60 per cent of their wages. At the peak of the development, in November 2009, 6,900 workers took this opportunity and left work to study or improve their skills. This was six times more than in November 2007 (BMASK 2010: 302).

3.3 Wages and working hours

For a number of years real wages have increased only very moderately in Austria, clearly lagging behind productivity growth. Even at the height of the recent expansion in 2007 a nominal wage hike of 2.5 per cent turned into a real wage increase of 0.3 per cent. Interestingly, the crisis year became a major exception in this long-term development. In 2009, real wages soared by an astonishing 2.9 per cent, which was as much as in the preceding eight years put together. Of course, the main reason for the boost in real wages was the fall in inflation (from 3.2 per cent in 2008 to 0.5 per cent in 2009), but even in nominal terms wages increased more during the crisis year than during the preceding boom (Hermann 2011). In terms of both nominal and real wage growth Austria was among the leading countries in Europe, ranked above countries such as Sweden and Germany. In fact, 2009 was the only year for a long time when wage growth actually exceeded the combined growth in average prices and productivity (Schulten 2010: 198). The growth in real wages was

instrumental in sustaining demand during the crisis and, together with the tax cuts, compensated for the dramatic fall in exports.

However, with the exception of the public sector, where the government agreed to an exceptionally high wage increase to maintain purchasing power (3.55 per cent nominally and 3.5 per cent in real terms in 2009), the growth in (real) wages was not necessarily the result of social partner consent and a common strategy to confront the crisis (Hermann 2011). In several cases the negotiations were particularly tense and temporarily broke down, especially in the spring 2009 bargaining round. The unions repeatedly had to mobilise workers to increase pressure on employers to accept wage increases despite the accumulating economic difficulties (ibid.). While Austrian unions strongly rejected employer demands for wage moderation, the electronics industry agreement contained a provision that allowed companies in economic difficulties – that is, companies that suffered a 15 per cent or above decline in turnover in the first quarter of 2009 – to increase wages by 1.4 per cent instead of 2.2 per cent. However, the provision was fairly controversial in the union movement and remained an exception (ibid.).

Working hours fell significantly during the crisis due to short-time working, the clearing of overtime accounts and the shift from full-time to part-time hours. But at the same time many workers continued to work overtime. According to Labour Market Survey data, average weekly overtime hours decreased slightly from 8.5 hours in 2008 to 8.1 hours in 2010 (ibid.). Consequently, both employer and employee interest organisations took the crisis experience as a reason to demand a reform of the working time regulation. However, while the employers' organisation pushed for further 'flexibilisation', including greater daily and weekly variation and the introduction of working time accounts, trade unions demanded a reduction of working time and the distribution of work among a larger number of workers (Allinger 2010; Hermann 2011). Both sides launched public campaigns to raise support for their position. However, as no side was prepared to make concessions the result was a stalemate and the continuation of existing regulations, which allow for comparatively long but collectively approved working hours.

4. From crisis to recovery – to stagnation?

After the contraction in 2009, the Austrian economy started to grow again in 2010. GDP grew by 2 per cent in 2010 and 2.7 per cent in 2011. The growth was driven by a strong recovery of export industry, fuelled mainly by the German upswing and sales to emerging economies, including China. However, growth slowed down again to 0.8 per cent of GDP in 2012, following a similar economic decline in Germany. Growth picked up again in the second half of 2013 and, according to preliminary figures, reached 2 per cent over the course of the year (0.3 per cent in real terms). According to economic forecasters, growth rates will remain slightly below 2 per cent in the coming years (Baumgartner, Kaniowski and Leibrecht 2014). Following the growth trajectory, registered unemployment fell to 6.7 per cent in 2011, but increased again to 7.0 per cent in 2012 (according to the Eurostat definition unemployment fell to 4.2 per cent in 2011 and increased to 4.2 per cent in 2013). Some sectors, such as the construction industry, continue to struggle with the effects of the crisis and a lack of new projects – even though the crisis has sparked investments in the housing market as an alternative to the stock market.

Recently, the economy has also suffered from a series of bankruptcies, including the liquidation of a major (Spanish-owned) construction firm with 4,600 employees and the insolvency of a major retail firm with 3,468 employees. Furthermore, while Austria still has one of the lowest unemployment rates in the EU, including low unemployment among young workers, many of whom are in vocational training programmes, a large part of the new jobs created since the crisis are part-time and not a few of them are short part-time. Hence the crisis has prolonged and accelerated the long-term trend of flexibilisation and precarisation, which has become an important feature of the Austrian labour market.

After exceptional real wage increases in 2009, collective bargaining also returned to the pre-crisis trajectory of moderate real wage gains. In addition, employers continued to step up pressure for the decentralisation of the existing bargaining system. As a result, the employers in the metalworking industry ended a 40-year long tradition of negotiating a uniform sector-wide agreement in 2012 and instead concluded separate agreements for the six sub-sectors. The subsectors are represented by distinct employer bodies, which are, however, all part of the Austrian Chamber of Economy. Initially, the new bargaining strategy sparked considerable conflict and led to a series of warning strikes. However, the

conflict was settled with the involvement of leading social partner representatives from the employer and trade union camps. Furthermore, in the end the differences between the six agreements turned out to be fairly insignificant and the PROGE and GPA trade unions won a significant wage increase (Allinger 2013).

Despite the austerity, the public deficit continued to rise in 2011 and 2012 and reached a high of 75.14 per cent in 2013, after which it is expected to decline (Schratzenstaller 2013). Austria thus exceeded the Maastricht cap of 3 per cent on new debt in 2009, 2010, and 2012 (*ibid.*). The government has subsequently increased efforts to cut spending without adopting a new austerity package. However, the future of Austrian public finances also depends on developments in the banking sector.

5. Continuing threats and unsolved problems

Austria has weathered the crisis relatively well. The recession was deep but short. Social partnership played a major role in mastering the crisis: trade unions and the employer organisations negotiated exceptionally high wage increases during the crisis and successfully pressed for a reform of short-time working which helped to maintain jobs during the downturn. In some respect, the crisis led to a revitalisation of Austrian social partnership. However, crisis corporatism quickly turned into competitive corporatism when the social partners started to defend subsequent austerity packages (see the contribution of Hans-Jürgen Urban in this book). The austerity packages were criticised by the trade unions but not challenged fundamentally. At the same time, wage agreements fell back to the pre-crisis path of very moderate increases and in 2011 they were even negative in real terms.

The banks and their engagement in central and eastern Europe presents a major threat to the public finances and future of the country. The liabilities of one bank alone (Hypo Alpe Adria), which was nationalised in 2009 because of insolvency, could cost the country 11.7 billion euros (approved by the European Commission as acceptable state support) and according to some worst-case scenarios even up to 17 billion euros.²

2. Der Standard, 11 September 2013, 'Hypo-Kapitalbedarf im Höchstfall 17 Milliarden', <http://derstandard.at/1378248815363/Hypo-Kapitalbedarf-im-schlimmsten-Fall-17-Milliarden-Euro>, accessed 12 September 2013.

Austria, furthermore, continues to be strongly dependent on the German market and the growth prospects of the German economy. In addition, growth prospects also depend on developments in Italy and central and eastern Europe, which are not only major trading partners but also closely interlinked through the banking sector (Italian investors own one of the largest Austrian banks).

Given the nature of the stimulus and austerity packages there is very little hope of a revitalisation and extension of the welfare state in order to counter the continuing *de facto* discrimination against women and low income earners built into the conservative welfare state model. New jobs continue to be frequently part-time and not a few are precarious. Hence female employment may continue to increase but at the cost of persisting gender inequality, especially with regard to male and female wages. The welfare cuts have aggravated rather than solved some of the most pressing social problems, including the organisation of long-term care or the labour market integration of disabled workers. Austerity and cuts in welfare benefits have further aggravated inequality.

As an OECD study (2013: 4) shows, despite the financial turmoil and stock market losses, the top 10 per cent of earners still increased their share more than the bottom 10 per cent between 2007 and 2010. Another study on the distribution of household wealth, published in 2013, showed that inequality in Austria is much larger than previously assumed: the wealthiest 5 per cent of Austrian households own almost half of gross wealth in the country, while the lower 50 per cent of households own a mere 4 per cent (Andreasch *et al.* 2012: 249). Despite growing inequality, the conservative forces in the 'grand coalition' government have blocked any attempts to increase taxes on capital and private wealth, for example on so-called private foundations that enjoy particularly low tax rates. Given the comparatively very low property taxes, even the OECD recommends a 'review of capital taxation' (OECD 2011: 26).

In sum, Austrian institutions have been helpful in rapidly developing and implementing anti-crisis measures. However, in doing so they have reinforced path dependencies, thereby blocking the adoption of more future-oriented strategies. As a result, the country seems to be in deadlock. On the surface Austria is doing comparatively well, managing to maintain growth and hold down unemployment. However, the alleged success story stands on shaky ground, such as growth in Germany and stabilisation of the situation in central and eastern Europe. Below the surface

the country faces a number of unsolved problems, including increasing labour market segmentation, growing social and gender inequality and a looming care crisis. In other words, while Austria seems to be able to hold on to existing achievements, it is not making the investments needed to cope with future challenges, including long overdue investments in public infrastructure and research, as well as in a profound social and ecological modernisation.

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Neoliberalism 2.0: crisis and austerity in the UK

Damian Grimshaw and Jill Rubery

1. Introduction

Four years into the austerity programme introduced by the Conservative-Liberal Democrat coalition after the 2010 election it is clear that the policy objective is to bring about fundamental change in the UK social model (Grimshaw 2014; Rubery and Grimshaw 2012), while neglecting the fundamental problems in the economic model that precipitated the 2008 crisis. This crisis was to a large extent the product of the UK model of capitalism, centred around financial services, credit-led booms and deregulated markets. This increased the model's vulnerability to the crisis, but the United Kingdom was also protected, compared with other European countries, from the ensuing sovereign debt crisis, notably by its position outside the euro area (euro zone) and its relatively long-dated government debt (which means less frequent debt resale). The policy direction post-2010 therefore represents at least to some extent a free political choice – that is, not directly dictated by the markets – but also one not mandated by the electorate. Labour lost but the Conservatives did not win the election outright and many of the changes introduced contradict manifesto commitments. This chapter assesses the changes that have taken place since the crisis, focusing in particular on the period of austerity policy, under three headings. We first consider macroeconomic policy up to early 2014, before and during the crisis and now under austerity; second, we look at the approach taken to the social model, including both welfare and employment regulation; and third we consider the approach to governance and the provision of public services.

2. Macroeconomic policy, banking crisis and response

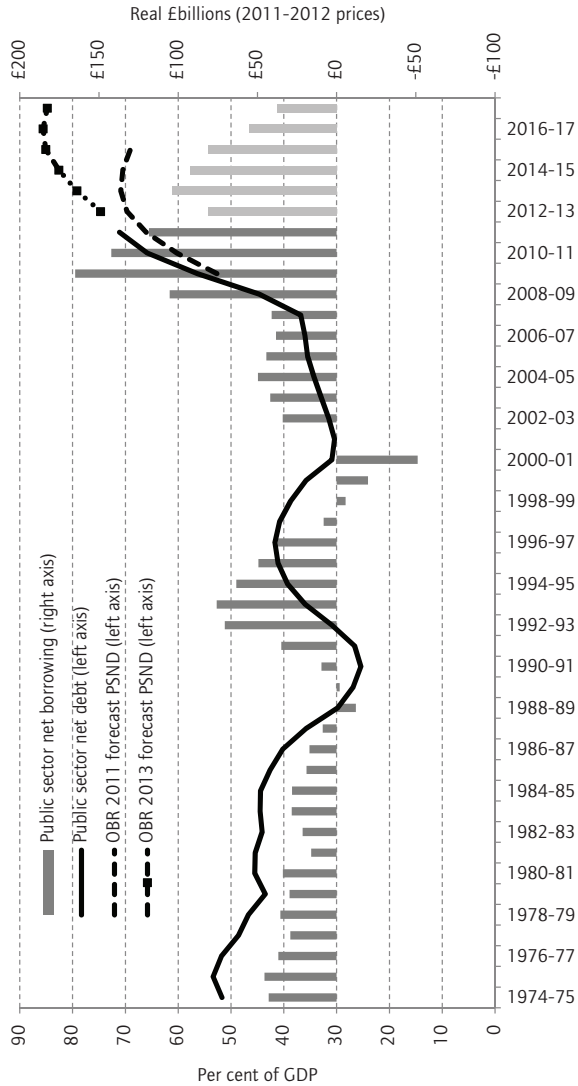
In the run up to the crisis, the UK economy was governed by a set of principles similar to those that govern the USA, namely, the pursuit of

low inflation, limited state assistance to firms and industries, ‘shareholder value’, deregulation of product markets and liberalisation of capital flows. At its heart, the UK model prioritised the interests of the rising class of finance capitalists. London has been an important geographical base for global finance. Moreover, Conservative and Labour governments have pandered to its needs, based on the rationale that free markets prosper better with a financial class that can act unhindered to help markets grow. While the Bank of England and the Financial Services Authority repeatedly recognised the risks, they are said to have failed to appreciate the new system-wide nature of market risk (Besley and Hennessey 2010; HM Treasury 2008). The UK economy thus experienced the conditions that, as is well known, led to the financial crash; that is, a glut of cheap credit now made available to many low- and middle-income households, a booming housing market, an under-regulated banking sector and a bubble of derivatives and futures trading among an increasingly highly paid and uncompromising financial elite (see Elliott and Atkinson 2008).

There are strong grounds therefore to agree with Crouch’s (2009) assessment of UK macroeconomic policy during this period as ‘privatised Keynesianism’; an increasing reliance on private rather than government debt characterised the growth model. Moreover, it conforms to a growth model that Lavoie and Stockhammer (2011) describe as pro-capital with weak wage growth, one that is based on neoliberal economic policy and a distributional policy that favours capital over labour (including the active promotion of labour market ‘flexibility’, residual welfare policy and weakened collective employment rights). The combined result is a falling wage share, growing personal debt, rising poverty and instability.

Despite the apparent flaws in the government’s pre-crisis approach to macro policy, its response to the 2008–2009 crisis and post-2010 design of austerity measures suggest that few lessons have been learned. The United Kingdom is likely to experience a ‘lost decade’ of stalled economic output and investment, falling real wages, growing debt and a resurgence of unsustainable asset bubbles. A first piece of evidence is the very slow recovery of GDP, combined with falling real wages. GDP tumbled by 6 per cent from the first quarter of 2008 to mid-way through 2009 and then took a full 17 quarters to recover to its pre-crisis peak, far longer than recoveries from previous recessions. Real pay (median hourly earnings) is down 9 per cent (2009–2014) and in 2014 was approximately equivalent to its 2002 level.

Figure 1 UK public sector net debt* (PSND) and net borrowing**, 1975–2011



Notes: * Percentage of GDP; ** Real £billions (2011–2012 prices).

Source: Authors' compilation from public finances data, sourced from the ONS/HM Treasury Public Sector

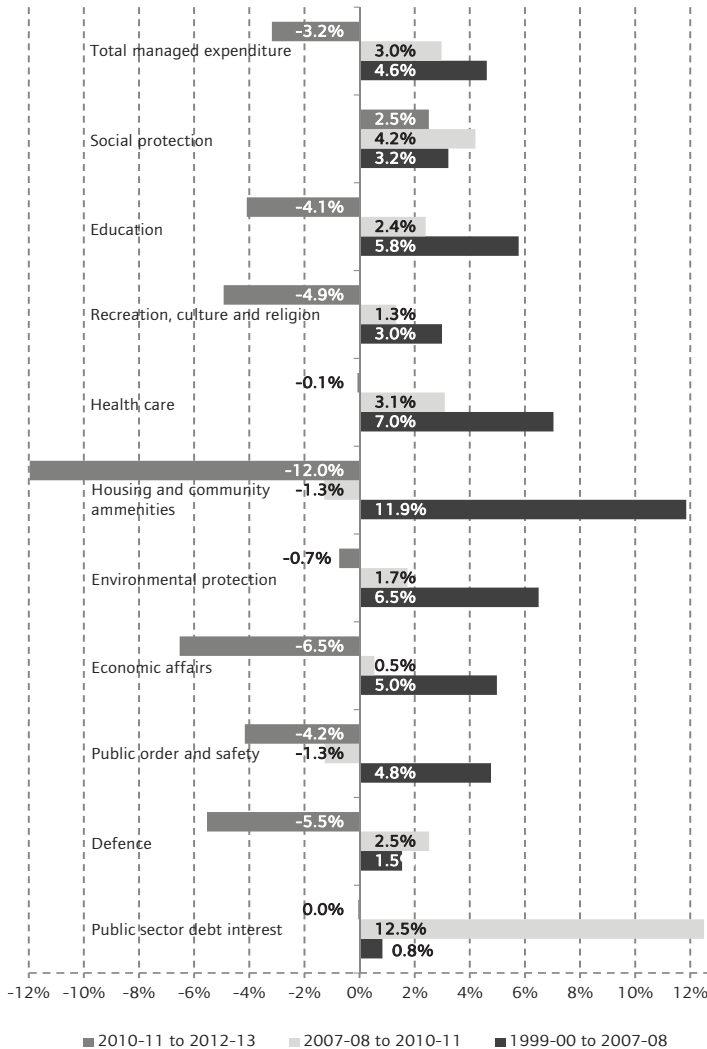
The pattern of falling real earnings applies to both male and female workers, to those in full-time and part-time jobs and to workers employed in the public and private sectors. Analysis by the Office for National Statistics (Levy 2013) shows that the steepest fall (2009–2012) was for male full-time workers in the private sector (9 per cent on average) and the smallest for female part-time workers in the public sector (3 per cent). However, in the course of the roll-out of public spending cuts since 2010 real pay cuts for full-time public sector workers have exceeded those for the private sector (2010–2012 data).

A second piece of evidence of Britain's likely lost decade is the repeated extension of the period required to achieve the planned reduction of the structural deficit and a turnaround in rising public sector net debt. Figure 1 shows how the government's independent Office for Budget Responsibility (OBR) has had to adjust its predictions in response to the slow recovery in GDP and lower than expected falls in net borrowing. In 2011, on the basis of OBR forecasts, the government was confident that debt levels would peak at 71 per cent of GDP in 2013–2014. The 2013 projections forecast debt levels continuing to rise to 86 per cent by 2016–2017, amounting to a three-year postponement of one of the government's central macroeconomic targets.

The government has not responded to real developments by revising its mantra about the need to cut public expenditures and investment in an effort to rapidly reduce deficit levels. Since 2010, spending cuts have been its centrepiece policy in an effort to eliminate the structural budget deficit and to reduce public sector debt (Treasury 2010). The extension of the forecast timescale required to turn around rising debt levels seems simply to have persuaded government that it needs to be resilient and to stick to the course by extending the period of spending cuts. Only with respect to investment spending has the government scaled back its planned reductions partly in response to lobbying from the IMF, among other organisations, that the cuts were damaging prospects for recovery.

Figure 2 compares the average annual changes in public expenditures for different areas of spending across three periods. During the three years of recession and partial recovery prior to the election of the coalition government (2007–2008 to 2010–2011) the New Labour government continued to raise spending, albeit at a slower pace than in the previous decade in the major areas of education and health care. As a direct result, jobs in the public sector increased by 92,000 from early 2008 to early

Figure 2 Average annual percentage change in real public expenditures over three periods: pre-recession, recession/recovery and austerity



Source: UK Treasury data, 'Public Expenditure Statistical Analyses 2013: Chapter 4', available at: www.gov.uk/government/publications/public-expenditure-statistical-analyses-2013.

2010, providing some compensation for the loss of around 790,000 jobs in the private sector.¹ From 2010 onwards austerity became the order of the day; spending cuts have already taken out around £45 billion of expenditures in real terms (a 6.3 per cent reduction in total managed expenditures from 2010–2011 to 2012–2013). The largest cuts are in defence, public order and particularly education (7.7 per cent), involving the scrapping of Labour’s ‘Building Schools for the Future’ programme, the continued shifting of university funding to students by forcing them to take out loans, cuts in youth services and reduced education budgets for 16–19 year olds. Social protection spending, despite a raft of radical “reforms” that have reduced entitlement and cut benefit levels (see below), has nevertheless continued to rise (by £12.2 billion over the two-year period), caused by a combination of the stalled economic recovery, rising numbers of households falling below the poverty threshold (partly a result of too many ‘lousy jobs’ among net jobs created in the private sector, which offer low pay and/or undefined working hours, so-called zero-hours contracts) and incompetent policy design by government, as is becoming increasingly evident in critical parliamentary and legal evaluations of post-2010 social policy reform (see below).

Spending cuts have been significantly hampering economic recovery. The government blames weak global markets but our analysis suggests that public spending cuts are causing much of the damage. Falling public sector incomes are not only depressing aggregate demand, but also causing a sequence of knock-on effects on the private sector through interlinkages of outsourcing, partnerships and subcontracting in the United Kingdom’s mixed economy. Moreover, it has proven to be a great shock to UK public services and to women’s prospects for quality employment (given their overrepresentation in public sector employment, see below), suddenly reversing more than a decade of average annual rises of 5 per cent in public spending. The implications of spending cuts vary significantly by region, such that areas outside London and the South East are facing significantly higher risks, fuelling perceptions among commentators that on a variety of economic indicators London looks increasingly like a different country.

1. The public sector data exclude workers employed in the banks that were nationalised (RBS and Lloyds in 2008); these data are instead included in the private sector data. Data refer to the 24-month period from the first quarter of 2008 to the first quarter of 2010 and derive from ONS data ‘Public and private sector employment’ and ‘Public sector employment including and excluding financial corporations’, available at: www.statistics.gov.uk/statbase/product.asp?vlnk=8284.

A third piece of evidence concerns the continuing instability of the UK model centred on an unreformed financial economy. The September 2007 run on the retail deposits of the Northern Rock bank was followed by an unprecedented £850 billion government bailout of the banking industry, an increasing number of house reposessions and rising unemployment. There followed a short-lived backlash against bank executives, including a highly publicised grilling by politicians of hedge fund managers and widespread criticism of ‘fat-cat’ bonuses in the City. However, the UK model’s neoliberalism reasserted itself in the policy response to public demands for stronger banking regulation; a widely anticipated government review, Project Merlin, concluded by supporting the status quo, arguing against a re-regulation of the banking industry and a tax on banks or on bonuses. Instead, the four largest British banks were merely requested to ensure that their 2010 bonus pool be lower than for 2009 (and only for their UK workforce); to agree lending targets to business (with more set aside for SMEs); to link lending targets to bonus payments; and to publish the pay of top earners. These have been subsequently monitored but the post-2010 period has not witnessed a significant change in speculative behaviour or high pay culture.²

Far more significant has been the radical policy measure known as ‘Quantitative Easing’ (QE), borrowed from Japan’s response to its 1990s asset bubble crisis. QE involves the purchasing of financial assets (largely gilt-edged securities or ‘gilts’), which are held mainly by insurance companies, banks and pension funds. Starting in 2009, QE amounted to some £375 billion by late 2013 (roughly equivalent to the UK’s annual GDP) and means that the Bank of England now owns around one-third of the gilt market. With interest rates at a historic low level, the Bank’s objective is to increase liquidity, restore confidence and encourage more lending by banks. However, the policy has met three main criticisms. First, pensions are likely, on balance, to have been adversely affected by QE. Funds that were already in deficit have fallen further into debt because rising gilt prices have reduced yields, and annuity rates on pension pots have fallen significantly (NAPF 2012). On one hand, this increases the burden on employers and existing employees to make up the shortfall, but also raises the real risk that pension fund holders will move out

2. Evidence includes: bank bonuses decreased by 8 per cent in 2010–2011, but basic pay increased by 7 per cent (*The Guardian*, 26/04/11); continued use of multi-million pound ‘golden hellos’ and salaries to banking board executives and non-board executives (High Pay Commission 2011: 31–32).

of gilts into more risky investments. Second, by encouraging the holders of gilts to sell and exchange for other financial assets the policy has indirectly supported a rising FTSE stock index, which at the time of writing is already disconcertingly higher than its pre-crisis peak level even though GDPs remains lower.³ Third, QE has had a very regressive effect on wealth distribution. In its evaluation of the distributive effects of QE, the Bank of England reports an overall boost to UK households' net wealth of approximately 16 per cent, but observes that 'in practice the benefits from these wealth effects will accrue to those households holding most financial assets' (2012: 10). Given that in 2011 the median household held an estimated £1,500 gross assets and the top 5 per cent of households an average of £175,000 it is easy to see the regressive impact of wealth changes. The Bank of England is quite clear in its conclusions:

By pushing up a range of asset prices, asset purchases [as a consequence of QE] have boosted the value of households' financial wealth held outside pension funds, although holdings are heavily skewed with the top 5% of households holding 40% of these assets. (Bank of England 2012: 21)

3. Towards a true neoliberal employment and social model

The austerity-related changes in the UK social model (encompassing both welfare and employment aspects) have both reinforced long-term trends and introduced a distinctive shift towards an ideal-type neoliberal model. This dual characterisation reflects the essentially hybrid nature of the United Kingdom's social model prior to the austerity programme and the hybrid and divergent trends observed under New Labour (Rubery 2011; Grimshaw 2013a). Thus while changes under New Labour reinforced the neoliberal principles of work discipline, deregulated labour markets and a flat-rate benefit welfare system providing minimum and often means-tested benefits, at the same time it introduced new social rights and higher social floors, which modified the neoliberal effects and reinforced the model's hybrid character. The main policies under New

3. This observation is taken from Cambridge economist Ha-Joon Chang's 26 July 2013 column in *The Guardian*, available at: www.theguardian.com/commentisfree/2013/jul/26/george-osborne-economy-orwellian-on-mend.

Labour that provided stronger social rights included extending statutory employment rights (most notably the national minimum wage), improving the level of minimum welfare benefits, increasing resources and support flowing to children (Dickens 2011) and to working parents (Wald-fogel 2011) and developing, albeit at a relatively low level, some active labour market programmes for the unemployed (Bonoli 2010).

While these policies together constituted a significant improvement in social rights, their implementation was still limited or directly influenced by neoliberal ideology (Rubery 2011). With the exception of the national minimum wage, the new statutory employment rights were limited primarily to those already agreed under the EU Social Charter and followed from the decision to renounce the opt-out from the Social Charter.⁴ The New Labour commitment to reducing poverty, particularly child poverty, while offering significant resources was, however, closely tied to the implementation of the policy that employment was the key solution to child poverty and thus went hand in hand with increasing imposition of pressure on lone parents to seek work. The extensive new forms of support for working parents were based on neoliberal market policy and a residual welfare model, so that childcare support was provided through tax credits but provision relied on high cost private suppliers; leave was extended but payments kept at low flat-rate levels; and the right to flexible working amounted to no more than a right to request it, thereby leaving decisions up to employers. The New Deal programmes for the unemployed retained the neoliberal doctrine that any work was better than no work, so that the ambitions for active labour market policies with regard to retraining or lifelong learning remained very underdeveloped. Finally, none of these policies were aimed at reducing inequality by applying measures affecting the top end of the earnings and wealth distribution.

This hybrid approach was also seen in New Labour's response to the financial crisis; it failed to increase unemployment benefit levels, or extend coverage, unlike France, for example (Gautié 2011: 231). On the other hand, it did provide some social support, notably through increasing child benefits and reducing VAT, introducing new schemes for young

4. Three exceptions to this ban on more employment regulation included the extension of paid holidays from 20 to 28 days, the development of leave and flexible working policies for working parents and, finally, the adoption of a UK-specific regulation on temporary agency workers.

people (particularly the youth guarantee scheme and the £1 billion Future Jobs Fund) and also, for the first time, raised taxes on the higher paid, to 50 per cent for those earning more than £150,000.

This description of New Labour policies before and during the crisis provides a benchmark for considering the extent of continuity and of change under the coalition government elected in 2010. We discuss these in relation to four main policy areas.

Welfare benefits and welfare-to-work policy

The key area of continuity and indeed intensification is the approach to work requirements for the non-employed dependent upon benefits. This includes continued and intensified pressure on lone parents and disability claimants to enter employment. Thus the age of the youngest child at which lone parents have to be ready to enter employment has been further reduced from 7 to 5 years and under the proposed Universal Credit system lone parents will have to begin to demonstrate work readiness from when their child is one year old. Furthermore all disability claimants are being reassessed for fitness to work by a test which to date has resulted in two-thirds of claimants being declared fit to work. However, a significant minority of appeals against the test have been successful, in May 2013 a judge ruled that the test discriminated against people with mental health problems (*The Guardian*, 22.05.2013) and in 2014 the private company administering the tests – the French IT firm Atos – quit the contract early because of damage to its reputation and brand. Disability benefits have also been cut and means-tested, with a particularly strong effect on women as they are more likely to have a working partner.

Another reinforcement of the neoliberal emphasis on work discipline is found in the now privatised job placement activities, called the Work Programme, where unemployed job-seekers may be required to take unpaid work (30 hours per week) or lose benefits. Negative press coverage led to major employers withdrawing from the scheme but, despite a court ruling that mandatory unpaid work was illegal, rules have been amended in parliament to allow it to continue.⁵

5. The Guardian 16/03/2013, p. 5 and The Guardian 22/03/2013, p. 12.

Alongside the reinforcement of work requirements, both the non-employed and those in work but reliant on in-work benefits have faced major cuts in the resources provided for them. There is no space here to list the dozens of policy ‘reforms’ that have cut incomes (see Grimshaw 2014; TUC 2013 for details). One area of reform that well illustrates the government’s anti-poor approach is housing benefits. The government has cut entitlement to housing benefits and their real value in the following ways:

- imposition of a 1 per cent cap on the annual uprating of housing benefits (as with all benefits);
- a reduction in the maximum benefit (from the 50th to the 30th percentile of local private rents);
- raising the age threshold for the right to seek individual rather than shared accommodation (from 24 to 34);
- a reduction of benefits for social housing tenants with ‘more bedrooms than needed’ (the so-called ‘bedroom tax’); and
- an overall benefit cap for working-age claimants (as part of universal credit reforms, 2013–2017) to be managed by reducing housing benefit payments.

In 2013 more than 20 London local authorities had already rented properties as far away as the North West and North East of England to transfer a rising number of low-income families out of London. The tax on ‘extra’ bedrooms is having greater effect in the north where more people live in social housing and is being applied even though there is a desperate shortage of social housing with one or two bedrooms. Some families are leaving social housing to be rehoused in smaller but more expensive private housing, thereby raising housing benefit payments still further (*The Guardian* 27.05. 2013). Moreover, very little is being done to resolve the underlying problems of a shortage of affordable housing and unregulated rents, which have boosted landlords’ incomes. The only silver lining is that the policy has been challenged repeatedly by vulnerable claimants. Late 2013 saw a court victory for a disabled tenant in social housing in which the judge argued that the definition of ‘spare bedroom’ was ambiguous and should not be applied to rooms used for the storage of equipment needed to live a normal life (*The Guardian*, 26.09.2013).

The benefit cuts are hurting those in low paid work as well as the unemployed; the government has increased the hours of work a couple with children needs to work before working tax credit can be claimed from

16 to 24 and has extensively cut both eligibility for tax credits and their value. In line with other benefits, the government has capped increases at 1 per cent until 2016. These policies are reversing the pattern of cuts compared with the initial phase of the cycle which affected middle to higher income families more; in 2015–2016 it is the poorest families who are forecast to face the biggest cuts (Brewer *et al.* 2013). The future plan is to move to a universal credit system to provide a more unified benefits and credit system. The need for simplification and for adjusting the high penalty thresholds that created work disincentives in New Labour's system is undisputed, but the proposed new system will create new barriers, particularly for women (WBG 2011), and is being introduced in the context of an £18 billion cut in the benefits budget even before the 1 per cent cap on increases.

Support for families, children and young people and gender equality

Turning to the second policy area – support for families, children and young people and gender equality – we inevitably find that many of the benefit policies described above are having a particularly strong negative impact on families with children, especially lone parent families (Browne 2011; Rabindrakumar 2013), who have been identified as the main losers from coalition policy changes. These changes are significant: it is estimated that without the positive flows of benefits related to children under New Labour, roughly one million more children would have been in poverty in 2007/2008 (Dickens 2011). These gains have rapidly been put into reverse.

The most important measures are changes to tax credits, particularly childcare credits and the freezing of child benefits. A particularly controversial change was the removal of these latter benefits from higher income families. Not only did this for the first time breach the Beveridgean principle of universal support for children but it also cut from households in which at least one member paid the higher rate of income tax (40 per cent on annual incomes of 41,000–175,000 euros). As many households have income above this threshold due to two earners and would keep the benefit, the policy appeared arbitrary and unfair and had to be revised before implementation, so that loss of benefits was staggered. This U-turn exemplifies the incoherence of the coalition's policy towards the family. In the first budgets not only were child tax credits savagely cut

back but also cuts to local government ensured that childcare provision (especially in low-income neighbourhoods) would also decline. In 2013, however, a new childcare subsidy was announced but this will primarily benefit middle to high income earners (up to a very high threshold), while child tax credits were more beneficial to low income households. However, these subsidies do not compensate for loss of child benefits by middle to high income households so no-one is satisfied.

State support for young people is also being cut in a range of areas, putting more pressure on families to support their children for longer. Many of the active labour market programmes axed by the coalition government are also related to young people, particularly the youth guarantee scheme. Those from low income households staying on at school have also lost the educational maintenance allowance, a means-tested benefit to provide support for young people to continue in education. For those entering higher education there has been a tripling of student fees to £9,000 per annum at most institutions. This extra burden will be felt by this age cohort primarily in the future as all fees are funded upfront by the government, but nevertheless the new system places a heavy extra burden on the current cohort of young people and, by extension, their families. Overall, real education spending per capita fell by 10 per cent during 2010–2013 (Grimshaw 2013). Young people are also a major target of the housing benefits cuts, with a raising of the age at which they can claim for independent accommodation instead of shared housing from 24 years of age to 34. This is expected to displace at least 60,000 young adults who claim housing benefits, to which the government minister responsible blithely responded that they should consider moving in with their parents (Shelter 2011). Already by 2012 homelessness was found to be rising particularly among young people (Fitzpatrick *et al.* 2012).

As women suffer disproportionately from cuts in both services and benefits, even disregarding the associated public sector employment effects (see below), the austerity programme is clearly reducing gender equality (Rubery and Rafferty 2013). This might be considered to be simply an unavoidable consequence of fiscal consolidation, but in several areas the coalition is signalling a direct change of approach. For example in preparing for the new universal credit (DWP 2011a, 2011b) the government has abandoned the long-standing tradition of paying benefits for children directly to the carer and instead insists that all household benefits be paid to only one household member, paving the way for a

major switch of resources from the (female) purse to the (male) wallet. This is despite research (for example, Sung and Bennett 2007) that shows that the current system is important for the well-being of children. The government defends its approach in terms of the sanctity of the family, stating that: ‘making decisions over household finances and budgeting in the most appropriate way to meet family needs is best done by the family itself. It has been suggested that Government interference in household budgeting arguably undermines individual responsibility’ (DWP 2011a).

The proposed Universal Credit will also reduce work incentives for second-income earners (mostly women) and over 2 million potential or existing second-income earners will see a rise in their participation tax rate from a range of 30–33 per cent to 45–65 per cent. This is defended on the grounds that ‘incentives for first earners have been given priority over second earners’ (DWP 2011b). In pursuing this approach it is failing to appreciate that reduced employment among second earners today will reduce the likelihood of employment participation tomorrow, for example, among those who become lone parents following the break-up of families (WBG 2011b).

This policy change is accompanied by major cutbacks in the already limited support for childcare and a decision to treat issues of childcare and women’s employment as an entirely private and family-based decision area, except for lone parents who, because they would be a ‘burden’ on the state are not allowed to choose not to work after the youngest child is five. The only positive policy in this area is the implementation of rights for shared parental leave; fathers have already been allowed to take up leave entitlements and statutory leave pay if the mother returns from maternity leave early and from 2015 maternity leave will be converted into parental leave that can be shared but there will be no additional rights for fathers and proposals to allow part-time leave that would have increased take up because statutory pay is very low have been dropped (IER 2013).

Support for the elderly

There are two main elements in policies for supporting older workers and the elderly; one is pensions, the other is social care. State pensions are very low in the United Kingdom, providing a replacement rate of

37 per cent, on average, of gross median earnings in 2011, compared with an OECD (34-country) average of 61 per cent (OECD 2011). Aware that support for the Conservative Party is stronger among the elderly, the government has protected current pensioners from many of the cuts (for example, the 1 per cent cap) and has restored the link to average earnings for the uprating of pensions, as planned by Labour. As earnings growth is very low, however, this has not yet brought improvements,⁶ but the coalition is also merging the basic and second state pension to form a flat-rate pension from 2016 (£7,488 pa in 2016), which should benefit future pensioners who have either spent long periods not in work – mainly women – and the self-employed, although many who would have claimed the second state pension will lose (Crawford *et al.* 2013).

However, future pensioners will have to wait longer for their benefits: the coalition has brought forward increases in retirement ages (to 66 by 2020, and 67 by 2026) and plans to link retirement age to life expectancy trends, so further rises can be expected. Little has been done to resolve the key problem of the closing of good quality occupational pension schemes in the private sector, which were central to the maintenance of living standards for the elderly, except to reduce the generosity of public sector pensions in the name of ‘fairness’. A new savings scheme has been introduced, again planned by Labour, but this provides for only very low contributions by both employees and employers and is not compulsory, although employees are automatically enrolled so have to actively opt out not to participate.

Elderly care provision has traditionally been relatively extensive in the United Kingdom, but has become less available as demand has increased. Most care is financed by public spending, although the bulk of care is provided by private sector (and some voluntary sector) organisations. Cuts in funding to local government – one-third reduction in resource spending over 2009/10 to 2014/15 – have had a particularly serious impact on elderly care provision and have required many local authorities to renegotiate the terms of outsourcing contracts with private sector companies and reduce levels of care entitlement. The core focus of government action in social care has been capping limits to private

6. In fact the policy change guarantees a rise equivalent to the larger of average earnings growth, the consumer price index or 2.5 per cent (referred to as the ‘triple lock’).

spending on care to reduce the costs of care for families due to inherit assets, but nothing has been done to increase the supply of care and to provide better pay for care workers, who are often paid the minimum wage and even illegally deprived of pay for work-related time, such as travel between clients.

Labour market regulation

With regard to labour market regulation the coalition has done much to reverse the policies of improving statutory minimum floors adopted by New Labour. Furthermore, reducing statutory employment rights is one of the key objectives of the Conservatives in renegotiating the United Kingdom's position in Europe. In practice, the coalition has not been able to dismantle two of the most important rights Labour established: first, the national minimum wage, as this has proved popular, although increases recommended by the Low Pay Commission during the coalition government's term of office have been below inflation; and second, the statutory entitlement to paid holidays (which increased from zero to 20 and then to 28 working days under Labour's watch and thereby significantly increased holidays for part-time workers), as this provision is covered by the EU's working time directive.

However, other rights have come into the coalition's firing line: New Labour reduced the period of continuous employment that applied in the case of workers' claims of unfair dismissal from 24 to 12 months but this was quickly reversed by the coalition. Also, from April 2013, the minimum consultation period for collective redundancies was reduced from 90 to 45 days for large-scale redundancies and workers on fixed-term contracts are excluded. Also shredded is the Two Tier Code that provided protection for new employees under outsourcing contracts from the public sector, requiring them to be paid at public sector wage rates, thereby enhancing the protection offered by the EU directive on Transfer of Undertakings. Abolishing TUPE regulations and the working time directive are top of the wish list for the Conservative Party in renegotiations with the EU. The further entrenchment of neoliberalism is starkly evident in the bizarre new policy (in force from September 2013) enabling the exchange of worker rights for company shares. This involves the creation of a new legal category of 'employee shareholder' who, among other things, has to give up rights to claim unfair dismissal, redundancy rights, maternity and adoption leave, flexible working and

so on, but take up is expected to be low. Perhaps the most negative development in labour market policy has been the introduction of relatively high fees that have to be paid by any employee taking a case to an employment tribunal; this turns human rights into market goods, as we discuss in Section 3.

3. The shrinking public realm

Taylor-Gooby and Stoker (2011) argue that the coalition is set to dismantle the so-called 'big state' and its institutions in such a way as to prevent its re-establishment by a new government of a different political persuasion. This involves a restructuring and considerable narrowing of the public realm in many dimensions. Three dimensions to this strategy can be identified: first, a rapid acceleration in the widening of the policy of privatising public services; second, a trend towards either abolition or commodification of citizens' individual or collective human rights; and third, a shrinkage and downgrading of what is left of the public sector.

Privatisation has been accelerated in the large areas of job placement (as already discussed), justice (including the probation service, some policing and prisons), health care and education. Health care has been subject to incursions from the private sector since the 1990s, particularly in the form of private finance investments in new buildings and ancillary services, but radical changes in governance structures under the coalition are expected to herald a massive expansion in the scope for private services involvement. Post-2010 reforms devolve responsibility for commissioning of an estimated £60 billion of health services to consortia of general practitioners (and much of the commissioning task itself will be subcontracted to private sector business services firms) that will have the task of making available to patients a choice of private and public sector health service organisations. Reforms will oblige these consortia to commission services from 'any qualified provider'. But the reforms are controversial; they were temporarily blocked in 2011 but were eventually passed with minor modifications. They continue to be opposed by the main trade unions and professional associations, who argue it will lead to profits being prioritised over care.⁷

7. See, for example, the statement by the trade union Unison, available at: www.unison.org.uk/acrobat/A11839.pdf

In education, most secondary schools (56 per cent in 2014) have been taken out of local government control due to incentives or even requirements on schools to adopt 'academy' status, which ties schools to central government accountability and, in addition, community groups are being encouraged to set up so-called 'free schools' outside government regulation, including the need to employ qualified teachers in all classrooms. There are strong grounds for expecting the next stage to be to allow these academies and free schools to be run by profit-making companies (leaked documents suggest that this is the secretary of state's plan, *Independent* 10.2.2013). Likewise the policy of ending state tuition subsidies for higher education is explicitly designed to open up the market for higher education to bring in 'for profit' providers.

The second line of attack on the public realm is the narrowing of citizens' individual or collective rights, a weakening of enforcement of rights or their conversion into 'liquid commodities' to be purchased only by those who can afford it. The narrowing of rights or weakening of enforcement is justified by the standard arguments for a 'bonfire of regulations'; examples include relaxing rules on planning permission and the restrictions of health and safety inspections to 'high risk' workplaces from 2013. The conversion of rights into commodities includes not only access to higher education, but now also access to the legal system as legal aid for the poor has been largely abolished and access to employment tribunals requires the payment of a significant upfront fee. This means in effect that recourse to the law is no longer a citizenship right and the ending of legal aid for family breakup will have major implications also for children. Another development is the restriction on choice of spouse for those without sufficient resources. Those who do not earn at least £18,600 per annum are not able to marry a non-EU citizen and bring them into the United Kingdom. This applies to 61 per cent of women, 58 per cent of young people aged 20–30 years old (Migration Observatory 2013) and undoubtedly to the vast majority of both men and women from ethnic communities. Social care is also being rationed increasingly, so that those with substantial needs may have no access except through private payment, even when they have limited resources. Access to many desirable areas of employment is also now increasingly conditional on being able to fund an unpaid internship, while those graduates who cannot do this face periods of unpaid internships in return for unemployment benefit, but in the most routine 'McJobs' rather than in blue chip companies.

The shrinkage and downgrading of the public realm is taking place along many dimensions. The shrinkage applies not just to the public sector but also to public support for third-sector organisations in the arts and charities sector and or semi-autonomous areas, such as universities, now reclassified as private sector organisations. This could soon happen to schools and hospitals as privatisation accelerates. Direct public sector employment is declining, reflecting both the growing privatisation and the expenditure cuts, particularly in local government (Grimshaw 2013b). Public sector employment is planned to decline by one million from 2011 to 2018 out of a total employment of just under five and a half million in 2011. The rate of job loss has been strong but is forecast to further increase from 34,000 per quarter to 36,000, so the worst is yet to come (OBR 2013: 76–77). The explicit government policy is to lower the level of terms and conditions in the public sector, particularly with respect to pay and pensions, but also working time (with much talk of the problems of the working time directive in restricting doctors' and hospitals' working hours and thereby operational effectiveness). Opportunities to employ non-qualified teachers in free schools can also be considered part of the denigration of professional public service work. These cuts will have particularly negative impacts on women, as they constitute the majority of the public sector workforce (Rubery and Rafferty 2013). It is legitimate to argue therefore that the coalition government's austerity measures have been strongly sex-biased.

Some of these policies are explicit – in particular, the downgrading of pensions and pay in the public sector – while others are imposed indirectly through, for example, major cuts to local government budgets, to shift the blame for the precise distribution of cuts to local politicians. Furthermore, restrictions on, or the commodification of, rights have gone hand in hand with further promotion of the 'consumer choice' agenda to justify radical 'reforms' in health and education. But of course choices under limited resources are not real choices. The stripping away of rights and services embedded in public sector and government institutions was legitimated in the early years of this government with reference to the development of a more informal 'big society', based around third-sector organisations and volunteers, ready and willing to fill in the gaps in services and to be more responsive to consumer needs. However, the widespread cuts to third-sector organisations and the continuing absence of any sign of an army of 'big society' volunteers led to a downplaying of this opportunistic rhetoric from 2012 or so.

So far resistance to these changes has been limited, possibly due to the uneven distribution of cuts, so that the complaints from the hard hit areas – which tend electorally to be Labour strongholds – can be ignored. Resistance briefly halted the health reforms, but the Liberal Democrats finally supported only moderately changed reforms rather than break the coalition, lending substance to the view that support from the Liberal Democrats has enabled the Conservatives to push through more radical policies than the electorate were willing to endorse. The outcome, according to the political writer and historian David Marquand, is that ‘the present coalition is the least legitimate peacetime British government of modern times’ (*The Guardian* 14.5.2011). During 2013 and 2014, the coalition government has sought to use critical reports of NHS performance to persuade the public of the urgent need for change and (implicitly) to support privatisation.

There is still active and lively criticism of the policy agendas and some movements to modify their impact – for example, a new national commission on living wages headed by the Archbishop of York and a series of public sector strikes and protest actions by public sector trade unions. Perhaps the most effective obstruction has arisen from the sheer neglect and incompetence of private sector providers and the clear inadequacy of public sector commissioning processes. Not only did the British army have to be drafted in to cover shortfalls in security for the Olympics but a whole raft of problems have arisen with providers withdrawing from contracts (for example NHS Direct, rail franchises), or being found guilty of systematic fraud and poor performance (Work Programme job placement services) or their behaviour and actions have been found wanting (for example, as already mentioned, 38 per cent of appeals against ‘fit for work’ assessments have been upheld, *The Guardian* 8.02.2013), while the private security firm G4S has been found guilty of causing unwarranted death during a deportation. Moreover, markets have failed to develop and deliver in accordance with government plans. For example, predictably, universities all set roughly the same student fees – the maximum – thereby failing to differentiate provision by quality. It is also certain that the markets being established in the NHS will not deliver what the government has promised. But the key question for the UK electorate is whether the re-establishment of an integrated and accountable NHS and a clear and extensive public realm will ever be possible, particularly in light of the proposed TTIP trade agreement.

4. Conclusions

The radical nature of the changes taking place and planned for the UK employment and social model cannot be overestimated. Under cover of the financial crisis a large-scale restructuring of the core institutions of the social and welfare model is taking place, involving not simply cut-backs in public expenditure but fragmentation of the organisations of public services, including health care and education, to clear the way for permanent and growing private sector involvement. Citizens' rights have been commodified or eroded, the size and status of the public services workforce downgraded and inequalities, particularly between men and women and between north and south, increased. In many senses the policies can be interpreted as an acceleration of well-established trends under governments of different hues, including the deliberate denigration of welfare recipients and the increasing coercion to work; the blurring of the public/private sector divide; and the flexibilisation of labour markets.

However, the new policy approach of the Cameron/Clegg coalition government can be considered distinctive in three respects; first, it is eroding many of the safety nets that in the United Kingdom have been more extensive than in, for example, the United States and were considerably improved under New Labour; second, it is withdrawing support from families and social care and explicitly reversing policies in support of working parents (albeit with some inconsistent policies to restore some marginal support); and third, it is extending privatisation into areas previously considered sacrosanct, notably health care, education and justice. The veil of macroeconomic necessity is steadily turning into an Orwellian ('Newspeak') excuse for a long-term squeeze as fiscal health has not been restored due to economic stagnation induced in large part by government cuts. The medicine prescribed is 'more of the same' so that the United Kingdom is at present set on a policy of austerity without end, which in turn may end even the pretence that the United Kingdom still has a social model.

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Coming to the end of the *via dolorosa*? The rise of selective economic nationalism in Hungary

András Tóth

The intertwining of a political crisis with crises of the economy and of public finances in Hungary began in 2006. Hard on the heels of this the global financial crisis let loose a veritable political storm. The upshot was that the FIDESZ party, with charismatic Viktor Orbán at the helm, obtained an overwhelming majority in the general elections. Orbán declared that, in accordance with the people's desire for change, he intended to instigate a revolution from which a new Hungarian model would emerge, superseding the previous one, which had been utterly discredited.

The first steps in this direction comprised five key areas of upheaval:

- (i) FIDESZ, which as an opposition party had strongly resisted any measures that they considered 'undemocratic', now proceeded to establish a regime sustained by an anti-liberal parliamentary majority that undermined or even completely eliminated the separation of powers provided for in the constitution.
- (ii) In its socioeconomic model the government set to work consolidating the position of the domestic elites and upper middle classes. It hoped in this way to launch a new development process shaped by domestic actors rather than by external ones.
- (iii) The government strove to establish the most 'efficient' labour market in Europe by introducing new, flexible labour market regulations and curtailing trade union rights.
- (iv) FIDESZ, which had previously vehemently opposed all cuts in social security, now switched to a policy of 'workfare' instead of 'welfare'. Unemployment benefit was cut sharply and social benefit recipients became subject to an obligation to work, which was supposed to end welfare dependency, although the payment for such employment was often extremely low.
- (v) Only in family policy was spending increased and welfare benefits

extended. Tax concessions were introduced for families with children in order to boost the long-standing very low birth rate and avert the impending demographic crisis.

FIDESZ hails this policy as a break with the ‘European model’, which it claims is doomed to decline, and has promised Hungarians a new, efficient ‘workfare’ state, which will bring the country out of the crisis. In what follows I give an account of what was achieved by this policy in its first four years and analyse a number of contradictions in the newly emerging Hungarian model. I begin the analysis with a brief look back at Hungary’s so-called ‘post-socialist’ model.

1. Rise and fall of the post-socialist model (1989–2010)

When the economic and political transition began in 1989 there were high hopes of the small and medium sized enterprise (SME) sector that had emerged from the semi-market economic system of the Kádár era and was now supposed to usher in a flourishing economy. Reality turned out quite otherwise, however (for more on the following see Neumann and Tóth 2009). In 1990, almost overnight, Hungary found itself having to contend with cutthroat competition in the global economic system. The effects of this stark exposure to competitive pressure were compounded by the disappearance of the former Soviet economic area. The introduction of a strict bankruptcy law made things even worse and accelerated the collapse of the state economic sector.

The precipitate introduction of a policy of glasnost led initially to a process of destruction. Large state companies vanished almost overnight. The storm was weathered only by firms bought by foreign investors or that serviced sheltered niche markets operated by state utility companies. The winding up of agricultural cooperatives led to a similar crisis in the countryside. The upshot was a social catastrophe. In the first years of the transition one quarter of the initial four million jobs were axed. Broad swathes of the population were driven from the labour market and made dependent on social benefits, especially the older generation, Roma and the low-qualified rural population. The employment rate has remained markedly below the EU average ever since (see Table 1); this at the same time imposed a heavy burden on the state budget (Fazekas-Scharle 2012).

The collapse of the state industrial sector had another, indirect effect. Because these companies had formed the basis of the former dual occupational training system, occupational training in Hungary was gutted. This loss has been woeful in terms of Hungarian industry's long-term international competitiveness. All the more so because the great expectations of an SME upsurge proved unrealistic. The SME sector was characterised by the fact that forty years under the Soviet system had left a stratum of people without capital or business experience who had been compelled to try to strike out on their own, rapidly founding start-ups from nothing. Most of the numerous new SMEs are micro-companies that serve the local market at a very low productivity level. Many of them are able to survive only on the basis of illicit employment and tax evasion.

Thus foreign direct investment (FDI) played a decisive role in bringing capital, modern technology and successful business models into Hungary. An FDI-based development strategy also suggested itself because since the 1970s the half-open character of the Kádár regime had enabled Hungarian businesses to establish many contacts with the West, which could now be put to use.

Attracting foreign investors went well to begin with. In the early 1990s Hungary was the destination of choice for FDI in central and eastern Europe (Hunya 1996). Thus in 1997 foreign investment per capita in Hungary was three times higher than in Poland and the Czech Republic. Hungary became an export location closely integrated in the European economic area, while most of the flagships of the Hungarian economy acquired foreign owners (Éltető-Sass 1997).

After years of painful adjustment in 1996 the Hungarian economy began to grow again. Together with rapid economic integration and the establishment of institutions oriented towards the *acquis communautaire*, this paved the way for Hungary's accession to the EU in 2004.

This rapid development was stopped in its tracks by the collapse of the rouble in 1998–1999, however. The ensuing economic slowdown coincided with a gradual restructuring and broader distribution of investment flows towards central and eastern Europe (Sass 2004). Tougher competition from other central and eastern European countries meant that Hungary lost its status as the main FDI location and the influx of foreign capital abated.

This led to a change of view among the general public and a change of direction in Hungarian economic policy. After years of growth Hungarians, encouraged by the forthcoming EU accession, wanted wages and living standards finally to converge with those in the rest of Europe. ‘Real harmonisation’ was demanded right across the political spectrum, including the trade unions. In an increasingly polarised party system the two main political camps resorted to populism in pursuit of votes.

FIDESZ, which had come to power in 1998, pursued a cautious economic policy up to 2000. This came under fire from the largest opposition party the MSZP (Hungarian Socialist Party). In order to avoid defeat in the 2002 elections the government hit back with massive stimulation of consumer demand. Public sector wages were raised by 75 per cent, the minimum wage by 60 per cent and a lavish programme in support of mortgage lending was implemented (which paved the way for the boom in private borrowing abroad and the catastrophe of 2008–2009, to which I shall return in due course). Although this was not enough to secure re-election for FIDESZ economic policy took a new course. In a bad-tempered election campaign FIDESZ and the MSZP sought to out-bid one another with calls for a ‘new social system’. The MSZP promised more wage rises in the public sector, a thirteenth-month bonus, the abolition of income tax for the low paid and an ambitious investment programme in infrastructure.

All this was implemented when the MSZP came to power. The expansive spending programme boosted the economy, but the increase in public debt now became a permanent problem. From 2003 the new government tried to curb spending again, but now FIDESZ resisted any cuts. Worried about losing votes in the forthcoming elections in 2006 the MSZP reverted to an expansive deficit-financed spending policy, led by new prime minister Ferenc Gyurcsány, a charismatic young politician. The MSZP won the 2006 elections easily with the slogan of the ‘Pannonian puma’, audaciously transferring the image of the ‘Celtic tiger’ to Hungary’s Danube basin.

However, now Gyurcsány had to comply with the European Commission’s demand that Hungary curb new debt in accordance with the Maastricht stability criteria. This sudden change of course in the direction of public spending cuts came like a bolt from the blue to most Hungarians. If that wasn’t bad enough a tape came to light of a speech given by the prime minister at a private meeting of the parliamentary party in which

Table 1 Economic indicators, Hungary, 1996–2013

	1996	2000	2005	2009	2010	2011	2012	2013
Economic growth (in %)	0.2	4.2	4.0	-6.8	1.1	1.6	-1.7	1.1
Employment rate	52.1	56.3	56.9	55.4	55.4	55.8	57.2	NA
Unemployment rate	10.0	6.6	7.2	10.1	11.2	11.0	11.0	10.2
Public debt (% of GDP)	72.4	56.1	61.7	79.8	82.2	82.1	79.8	77.8

Source: Eurostat.

he admitted that the government had 'lied morning, noon and night' to deceive the voters with falsified statistics about economic progress. Naturally a scandal ensued, with protests throughout the country and unrest on the streets of Budapest. FIDESZ accused the MSZP of election fraud and demanded new elections. The government refused and instead switched to a quasi-neoliberal reform programme. This gave rise to so much public criticism that a FIDESZ campaign for a referendum on the reforms bore fruit. The referendum held in spring 2008 gave FIDESZ an enormous boost as the party that promised to defend the welfare state against neoliberal deregulation.

The onset of the global economic and financial crisis in 2008 dealt the final blow to the MSZP government. The export-driven engine of the Hungarian economy stalled. GDP plunged by 6.8 per cent in 2009 and Hungary had to turn to the IMF for financial assistance, which forced it to implement harsh austerity measures in return (see Table 1). After years of growth driven by government spending the crisis only got worse as anticyclical measures were now off the agenda.

The crisis also exacerbated the problem of high foreign indebtedness. Since the prospect of EU accession had become real and especially since accession itself mortgages in foreign currency had grown rapidly, especially with Austrian and Swiss banks. By 2008 the borrowings of private households in euros and Swiss francs had reached 20 per cent of GDP. In the financial crisis from 2008 the forint exchange rate collapsed, strongly affecting that part of the Hungarian middle class that had taken out loans in foreign currency. Rising mortgage payments led to a collapse in private consumption, which in turn meant falling state revenues and

an increase in the budget deficit. They were mutually reinforcing, which hit the domestic economy hard. It was natural to attempt to escape from this trap by promoting exports through devaluing the forint and cutting wages but this had its drawbacks. High private debt in foreign currency put limits on devaluation of the forint if the livelihoods of large parts of the middle class and even greater turbulence in the domestic banking sector were to be avoided.

During this period FIDESZ launched a campaign to delegitimise the government and set out on a collision course with implementation of the measures demanded by the IMF and the European Commission. Their claim was that once the neoliberal and corrupt politics of the post-communist left was stopped dead in its tracks a new period of strong growth could begin. Viktor Orbán cast himself as the spokesman of a general discontent, but it was not clear in what direction he really wanted to take the country (Hörcher 2014). FIDESZ won a landslide victory in the 2010 elections. Winning just over 50 per cent of the votes was enough to give it a two-thirds majority in parliament. The MSZP lagged far behind and the third-placed party was the right-wing extremist Jobbik.¹ Thus began what Tóth, Neumann and Hosszú (2012) called the ‘conservative revolution’.

2. The new political model: charismatic ‘government by decree’ in a democratic guise

Since 1989 Hungary’s political system has been characterised by a constitution and electoral law that emerged from the so-called ‘velvet negotiations’ between the Communist Party and the democratic opposition before the first free elections. The aim of the constitution was a system based on separation of powers and oversight prerogatives on the model of Western democracies, while the electoral legislation was intended to enable stable government, which gave an advantage to the party receiving the most votes (Bozóki 2002). This favoured the formation of a system based on two parties or party coalitions contesting power. This

1. This majority was largely maintained in April 2014. FIDESZ obtained 44.5 per cent of the votes, which sufficed to retain the party’s absolute majority, enabling it to alter the constitution (133 out of 199 seats); the MSZP as part of a centre-left alliance is, with 26 per cent, only a little stronger than the right-wing extremist Jobbik, on 20.5 per cent. The Green-Liberal LMP, as in 2010, obtained a little over 5 per cent (Batory 2014).

two-party situation was further entrenched by institutional positions of power, influence exerted via networks, financial resources based on public funding and probably also by corrupt practices in an oligarchy-like intertwining of political parties and big business.

In this party system there is a gulf between right and left. The main party on the left is still the MSZP, a reformed and democratised successor party to the former ruling Communist Party. One consequence of this is that many observers question the MSZP's legitimacy as a truly democratic party. Even many liberals and Greens, not to mention others on the left tend to keep the MSZP at a distance (Tóth 2013a). It is true that since 1989 the MSZP has ditched the old Communist Party lingo and adopted a pro-European programme combining a universalist welfare state and acceptance of the market economy. This mixture, similar to the New Labour's 'Third Way' in the United Kingdom, was in keeping with the party's nature as an organisation of left-leaning reformist technocrats from the middle ranks of the former regime. The market economic orientation was also reinforced by that fact that from 1994 to 1998 and again from 2002 and 2008 the MSZP governed in a coalition with the liberal SDSZ.² This coalition consolidated the neoliberal tendency in the MSZP, even though from 2002 to 2006 they pursued rather a Keynesian policy based on expansive public spending. The two parties were always at one in their secular and non-nationalist stance, with a strong inclination towards Europe and an emphasis on democracy, political correctness, human rights and multiculturalism.

The strongest party on the right was originally the MDF, which formed a coalition with various other right-leaning parties in the first freely elected government. It was split from the start into a liberal-conservative wing and a plethora of right-wing clerical, nationalist and even anti-Semitic tendencies, which regarded the SDSZ as dominated by Jews. After the death of the first prime minister, József Antall, the right-wing increasingly gained the upper hand in the party, finally leading to its break-up in the mid-1990s, riven by internal disagreements. FIDESZ, with its firmly anti-communist and anti-MSZP orientation now became the leading force on the right. Under the leadership of Viktor Orbán they articulated

2. The two partners didn't really hit it off because in 1989 the SZDSZ had emerged from an anti-communist movement, while the MSZP comprised mainly traditional left-wing tendencies. However, the electoral system and the anti-left and anti-liberal pressure from the right reinforced the coalition, which became a left-wing-liberal camp in public discourse.

the defence of national interests and domestic employers over against foreign influences, including rejection of the takeover of state companies by foreigners through privatisation. FIDESZ was committed to state-led economic development, combined with Christian-conservative views on culture and lifestyle.

This split into a religious, conservative, nationalist and statist camp, on one hand, and a liberal, market-economic and pro-European camp, on the other, was one source of the polarisation in Hungary's political life (Körösi 2012). Both sides associated the other with all the wrongdoing perpetrated since the 1930s. A kind of cold war has developed between the two sides in which each side reproaches the other of operating an oligarchical system of political corruption to finance its re-election.

The two blocs have been galvanised by the dramatic events that have unfolded since 2006. The sudden turnaround of the MSZP and the revelation of Gyurcsány's overfrank speech led to political upheavals that far exceeded what might have been expected in a crisis. The MSZP lost its credibility in all the three areas that previously had been so important to it: the welfare state, democracy and technocratic competence. Exacerbated by a series of prominent corruption scandals the loss of trust came to encompass the democratic system itself.

FIDESZ seized its chance and criticised the domination of a 'post-communist' elite that had thwarted all hopes of change in Hungary. The oligarchic and corrupt system of government provided no institutional opportunity to get rid of a duplicitous government. The president must therefore be given greater powers to solve such problems.

FIDESZ itself became radicalised in this process and developed a view of democracy whose right-wing populist roots go back to interwar Hungary. Viktor Orbán fused the various right-oriented ideologies with the promise to revive the country from the ground up. This vision is based on a strong state that purports to unite society and protect it from foreign powers and their Hungarian fellow travellers. After his election victory in 2010 Viktor Orbán declared the launch of a period of revolutionary transition in which a new social contract and a 'system of national cooperation' would overcome the turmoil of the past 20 years.

The two-thirds parliamentary majority that was sufficient to alter the constitution enabled the new government to free itself of any constitutional

shackles and to make the law an instrument of government rather than a means of holding it to account (Tölgyessy 2011). A new legal order was fashioned whose aim was to undermine the separation of powers and government oversight. The new constitution, the limitations imposed on the Constitutional Court and the new media law – all passed without opposition consent – represent a break with how things were done before 2010, when all the major parties accepted the legitimacy of the constitution and acted accordingly. The power of the government was further reinforced by a policy of crowbarring loyal party men and women into key positions in institutions that are formally independent of the government. Finally, changes in electoral law have improved the chances of the incumbent government remaining in office (Tóka 2013). As the outcome of the elections in April 2014 shows, the government has changed the rules of the game to such an extent that elections in Hungary are now ‘free, but not fair’ (Batory 2014).

The government implemented a recentralisation programme in education and public services, as a result of which local control was weakened or even eliminated. The government has also gained control over most media outlets, with the exception of one or two independent TV channels. International organisations, such as Reporters without Borders, have criticised the curbing of press freedom and the witch hunts by means of which government control of the media was achieved (Reporters without Borders 2014). In a survey 48 per cent of journalists stated that press freedom had been curtailed and 34 per cent that they practised self-censorship (Mérték 2014). The idea is for a new cultural elite to drive left-leaning, liberal or multicultural ideas out of public life (Alföldi 2014).

The institutional overhaul of relations between employers and employees is also designed to curb the influence of independent actors. The government abolished the tripartite negotiating body, with its statutory rights, and replaced it with a tripartite consultation committee, in which NGOs and churches may also be included. Only employers and trade unions from the private sector are represented in the new committee; in the public sector there are practically no national negotiating structures any more. For some sectors ‘chambers’ have been established that are supposed to represent employees. At the same time, public sector trade unions have been frozen out, for example, by making it practically impossible to call a strike legally. The new labour code has also sharply curtailed trade union rights beyond the public sector (Tóth 2013b).

All these changes have led to the establishment of an ‘omnipotent government’ (Mises 1944), practically beyond legal control. And even if a conflict does arise between the law and government intentions the law can simply be changed.

For all that, the significance of the ‘Orbán phenomenon’ (Hörcher 2014) cannot be underemphasised. The charismatic prime minister conflates diverse right-wing traditions and tendencies into one policy line. The press is full of reports that Viktor Orbán himself develops the policies and strategy of the parliamentary majority, personally decides on all issues that he considers important and makes sure that all key organisations and institutions cooperate smoothly with the parliamentary majority. He has obtained a majority that no longer needs to reach agreement with other political forces (Fricz 2012). This new approach is expressed unambiguously by leading FIDESZ politicians. Parliamentary speaker László Kövér, for example, one of the key figures in FIDESZ, considers it a scandal that the MSZP is still in parliament (Kövér 2012). Although the new system takes its democratic legitimacy from regular elections crucial democratic rules are bent so systematically that they favour only the ruling party.

The charisma of the leading personality is the outward form of a majority rule that, although democratically elected, is anti-liberal and not open to any compromise. The elections of April 2014 showed that although this system is not supported by the majority of people, it can muster sufficient votes to maintain power.

3. The new economic model: selective nationalism and selective welfare state

In the discourse of the political right the prominence of multinational companies in Hungary was the result of the left-wing liberal economic policy that allegedly served foreign interests.³ The condemnation of capitalism and of the Western model became an increasingly important theme in Orbán’s speeches (Tölgyessy 2013). When FIDESZ was still in

3. For example, in a speech Viktor Orbán asserted that ‘the “Labanc” and their masters reshaped Hungary in the way they wanted in the name of free markets’ (Orbán 2014). The term ‘Labanc’ designates the Hungary that, during the period of the Habsburg monarchy, defended Austria’s interests over against those of its countrymen who advocated Hungary’s independence. q

opposition it deployed a neoliberal rhetoric and distinguished between value-creating and exploitative capitalists. The party posed as the defender of ordinary people in Hungary against exploitation by oligarchic capitalism. The crisis of 2008/2009 led to more disillusion with the 'Western model' and the 'lean state' and confirmed FIDESZ's criticisms of the path Hungary had taken since 1989. After the election victory in 2010 the party began a 'war of liberation' against both the 'post-communist oligarchs' within the country and banks, multinational companies and European and international institutions outside Hungary (Hörcher 2014).

FIDESZ's economic policy approach can best be described as 'selective nationalism'. Economic nationalism is a notorious form of state protectionism used to shield domestic economic actors from the effects of the world market by such measures as protective tariffs (Pryke 2012). Needless to say, Hungary's membership of the EU prevents it from going the whole hog in this respect, especially because it is a small, heavily indebted country with no strong domestic companies. In these circumstances it is not realistic to pursue an import substitution policy by means of tariffs with a view to building up national champions. Rather the economy is dependent on the exports of companies in foreign ownership that are integrated in global supplier networks. Against this background FIDESZ has opted for *selective* economic-policy nationalism: this is applied above all in certain protected sectors, but not in industry or in private sector business services.

In the latter two sectors the government pursues a neoliberal-leaning policy. It actively supports new FDI projects and for this purpose has concluded a series of strategic agreements with key investors. The new labour code purportedly has the aim of creating the most competitive labour market regulation in Europe and making it easier for multinational companies to pursue 'flexible' forms of work and employment (Tóth 2013b). Even the cuts in various social benefits and services can be seen as an attempt to propel Hungary in the direction of a neoliberal 'workfare' model. The most important measures in this area were the cutting of the period of entitlement to unemployment benefit from nine to three months, the ending of early retirement opportunities and cutting state payments for the abovementioned compulsory labour performed by the unemployed.

Economic-policy nationalism, by contrast, is applied to public utility companies, the retail trade, the banks and in sectors dependent on

government contracts. This includes many services provided by private companies for state or municipal authorities, but also calls for tenders for projects financed from EU funding, for example, in construction.

In these sectors the government does its best to reduce the role of foreign providers and to promote domestic companies.⁴ The first instrument it uses is to reinforce state influence among utility companies. It has invested a sum of around 2 per cent of GDP to renationalise numerous companies (Kester 2013a and 2013b). The second instrument comprises targeted tax increases for large companies, which are generally in foreign ownership (which clearly conflicts with the abovementioned strategic support for foreign investors). Furthermore, these special taxes form an important revenue source for complying with the European Commission's fiscal guidelines. Thirdly, and finally, by means of tough regulations a series of private companies have been transferred from their owners at a low price to either the state or to private domestic bidders within the framework of a state tender procedure (Index 2014; Kester 2013c).

One of the government's aims is to restructure particular economic sectors and to promote new domestic key companies. Part of the reason for this is to break the dominance of the former communist cadre elite in the Hungarian economy. According to many observers there is an oligarchy that was able to transform political into economic capital and thereby consolidated the corrupt structures of the past (Teller 1991), which led Hungary to economic catastrophe after the change of system. Thus major efforts have been made to replace the economic elite, especially in sectors in which business success depends on public contracts. It seems that one outcome of this is to have weakened the economic base of the MSZP so that it finds it even more difficult to compete with FIDESZ on an equal footing in elections. Finally, the restructuring of economic actors also serves the purpose of creating a new stratum of companies loyal to FIDESZ. Thus a group of companies that in 2009 won one-third of tenders, two years later won only 7 per cent of them, while another group of companies managed to increase its share during the same period from 9 per cent to 27 per cent (Fazekas and Tóth 2013).

4. The government regards, for example, a banking sector dominated more than 50 per cent by foreign owners as 'unhealthy' (Portfolio 2013).

Also part and parcel of this selective economic-policy nationalism is the deliberate consolidation of the upper middle class. The introduction of a general flat-rate tax of 16 per cent considerably reduced the tax burden on the topmost decile of tax payers. By contrast, the tax burden has increased substantially for everyone else, especially for those on low incomes. One particularly important measure designed to improve the financial health of this clientele was to eliminate high debts in foreign currency. As already mentioned, the many mortgages taken out in euros or Swiss francs had considerably restricted the scope for a monetary policy aimed at boosting exports. The government thus decided – in the teeth of strong protests from the affected banks in Austria and Switzerland – to repay such loans by means of a one-off payment at a forint exchange rate around 30 per cent below the prevailing market rate for euros and Swiss francs. According to estimates, one in ten households indebted to foreign banks had sufficient savings to be able make use of this opportunity and debt repayment in foreign currencies was reduced by around a quarter (ECFIN 2014: 32). Thus those parts of the middle class in the best financial health were able to avoid the fate of ever higher mortgage repayments due to successive devaluations of the forint, while the remaining risk of default – also for the domestic banking sector – continued to grow.

As already mentioned, selective economic-policy nationalism has a social policy counterpart. In order to maintain broad assent among the population the government has cut social benefits and services selectively. In practice, this means that in some areas – such as unemployment benefit and early retirement – severe cuts have been made, while other areas have not been affected. For example, the pension level and tax concessions for families with children have been maintained.

Selective economic-policy nationalism is manifestly contradictory and comes at a price. It can work only if there is a strong state; however, arbitrary economic-policy decisions undermine trust in the legislator and state institutions. Targeted tax rises for certain areas of the economy have contributed substantially to raise state revenues, but on the other hand they deter potential investors. How thin the ice is on which the government is skating is clearly indicated by the move with which the government improved public finances in 2011, at least for the time being. During the to-ing and fro-ing in economic and social policy around the turn of the century, outlined above, a new pension insurance pillar was introduced, based on compulsory contributions to additional pri-

vate insurance. In 2011 these private pension funds were renationalised by de facto compelling insurees to transfer their insurance policies to a special state fund (Financial Times 2010; Economist 2010). This gifted the public budget such a large additional one-off revenue that the budget deficit, which in 2010 had been -4.3 per cent, was transformed into a surplus of $+4.3$ per cent in 2011 (in 2012 it fell back to -2.0 per cent; ECFIN 2014). This additional revenue was important not only politically, enabling compliance with European Commission demands for deficit cuts, but also because it financed the abovementioned renationalisation of public utility companies and made possible the launch of state spending programmes.

The role of the state is all the more important the lower the contribution of the private sector to economic growth. Since the beginning of the economic and financial crisis the share of investment in GDP has been at its lowest level for a long time. The main contributors to the investment slump are construction and real estate; investment is picking up only in manufacturing industry. However, this depends primarily on investment decisions by large automobile companies, taken some years ago (ECFIN 2014: 37). The strain put on banks by the collapse of the real estate market also entails restrictive lending, in particular to domestic SMEs (IMF 2013).

The Hungarian National Bank, now led by the architect of the new economic policy and former minister of the economy György Matolcsy, plays a key role in the efforts to counteract this stagnation. Since 2013 the Bank has been implementing a radical low interest rate policy to stimulate lending and – for the purpose of boosting exports – to drive down the forint against the euro. The National Bank even has a lending programme for SMEs to overcome the restrictive lending in the private banking sector. The programme offers loans at below the market interest rate and a volume of 9 per cent of GDP (Portfolio 2014a).

Another lever of economic growth is government stimulus for the construction industry. A key component of economic recovery in 2013 was the avalanche of public construction contracts financed primarily by much more enthusiastic resort to European funds (Portfolio 2014b). The construction sector is thus booming again – albeit starting from a low level – although residential construction remains in the doldrums. However, wages are low and in other parts of the private sector employment growth remains weak. Overall, the structural problems of the Hungarian

economy compared with the decade before the crisis remain unchanged – especially the division between export-oriented FDI bastions, on one hand, and precarious, domestic market oriented SMEs, on the other, which pay low wages, avoid taxes and are characterised by a lack of capital and innovation. The spillover effects of the large foreign industrial companies on small domestic companies are modest, even after 20 years of FDI-based industrial development (ECFIN 2014: 51). Thus the financial basis of the state remains precarious. The government debt ratio is receding somewhat, but remains the highest in central and eastern Europe (even though it is below the EU average). Furthermore, the use of part of the resources acquired through the transfer of the private pension funds to the state budget for the purposes of current economic policy harbours considerable long-term risks for the statutory pension system (MNB 2010).

4. Outlook: the fable of the grasshopper who starved in the winter

Because of its precarious value creation base the Hungarian economy has been pursuing a growth path since the end of the 1990s that is more and more dependent on both public and private debt. The bursting of the real estate bubble, which had been inflated by loans in foreign currencies, imposed onerous losses on the middle class in particular. For the majority of the population low wages made the crisis even harder to bear than in many other European countries. What really stands out in how the situation has developed in Hungary, however, is the profound upheaval in the political system, instigated in tandem with the crisis.

Amidst this double crisis, under the leadership of Viktor Orbán traditional right-wing, racist and national-chauvinist tendencies have coalesced with resurgent anti-neoliberal and even anti-capitalist attitudes. The charismatic prime minister embodies the promise of a rebirth for Hungary, which has given him overwhelming electoral success, sufficient to enable the ruling party FIDESZ to change the constitution. This majority has been used in short order to reorganise the political system and to provide the government with almost unlimited power beneath a democratic cloak.

This power is being used to pursue a selective nationalism in economic policy, which combines targeted promotion of domestic companies with

neoliberal labour market reforms, designed to keep foreign investors coming. For all that the government's overarching strategic goal is to enhance the independence of the Hungarian economy in relation to foreign influences and to fashion a new economy dominated by the government and economic actors who are hand in glove with it. According to one apologist for the new regime the idea is to bring the colonisation of Hungary to an end. After the debacle of a market economic model steered by private interests, on this view, the government needs to create a new, strong state. The recovery of sovereignty also entails ending the one-sided dependence on the West and striking a balance between West and East (Zárug 2011).

In 2012 then minister of the economy Matolcsy talked of Hungary's economic development as a fabulous success story. Unfortunately, it may prove to be a fairytale in a different sense. One of Aesop's fables is about a grasshopper who spent the summer months singing to his heart's content instead of laying up provisions for the winter and so faced starvation when the seasons changed. The contradictory economic policy of the Hungarian government frightens off foreign investors, notwithstanding that same government's attempts to attract them by deregulating the labour market and weakening the trade unions. A strategy aiming to heal the split in the economy between FDI and domestic SMEs – in other words, a switch from a low road to a high road strategy – must be founded not least on a much higher level of skills, which requires extensive public investment in particular in training and further training (Neumann/Tóth 2009). Nothing of the kind is even on the horizon. Instead, the weak value creation potential of the domestic market-oriented economy, the low wages and labour market deregulation have brought the state's tax base to the brink, a situation rendered even more precarious by the long-term threat to the pension system and unfavourable demographic developments.

The success, for the time being, of Hungary's new dual model – 'government by decree' by a strong state to promote a selective economic-policy nationalism – after having emerged from a dual crisis, could have important ramifications for Europe as a whole. It shows that economic nationalism can win popular support, enabling a party or coalition to achieve and then cement power. Hungary is a relatively small country. In a larger EU member state, however, this combination of economic and political nationalism in democratic guise could pose a serious threat to the European project.

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The Swedish model in times of crisis: decline or resilience?

Dominique Anxo

1. Introduction

In the mid-2000s, my colleague Harald Niklasson and I published an article, 'The Swedish Model in Turbulent Times', which retraced the main developments of the Swedish model from its inception in the early 1950s up to the early 2000s (Anxo and Niklasson 2006). Our main conclusion was that, at the turn of the century, the Swedish model appeared *more* in line with the core components of the original Swedish model¹ than during the decades 1970–1980, which constituted, in our views, a clear deviation. During the 1990s, the economic policy modifications towards more restrictive and anti-inflationary macroeconomic policies, the re-orientation of active labour market policies towards supply-oriented measures and the structural reforms undertaken in wage formation, tax and social protection systems suggested a revival of the Swedish model. After a period of turbulence related to the early 1990s economic crisis, the Swedish economy underwent particularly favourable economic development. Up to the current global recession, unemployment oscillated between 5 and 6 per cent, inflation was curbed and current account and public finances were restored.

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1. Namely, a macroeconomic policy combining full employment and price stability, a centralised and coordinated wage bargaining system and the application of a wage norm, the so-called 'solidaristic' wage policy based on fairness (same wage for the same job independent of the profitability of the firm/industry) and efficiency (that is, fostering rationalisation at the company level and promoting productivity-enhancing structural changes through closure of unproductive plants). Last but not least the implementation of an ambitious countercyclical Active Labour Market Policy (ALMP) favouring occupational and geographical mobility. Low unemployment and full employment are to be secured mainly by supply-oriented ALMP programmes favouring a reallocation of the labour force from the declining parts of the economy to the expanding ones.

Although the re-orientation of macroeconomic and employment policy during this period might explain the ‘Swedish success story’, we stressed that the modifications in Swedish industrial relations – in particular, the clear tendency to a re-coordination of wage bargaining – without doubt played a vital role in the Swedish recovery. These new developments reflected a desire on both sides of industry to again coordinate collective bargaining at industry level and restore the leading role of the traded good sectors in wage formation. The tendency towards a resumption of coordinated collective bargaining co-existed with a marked tendency to decentralise and individualise wage setting and working conditions.

We also claimed that strong trade union organisations and high union density at company level ensured the implementation of negotiated forms of individualisation and differentiation (*negotiated flexibility*). In our view, these tendencies should not be interpreted as a weakening of the Swedish collective bargaining tradition, but rather as a recomposition and adaptation of the Swedish model of industrial relations in the face of the major transformations of work organisation and production processes over recent decades. In our view, these developments did not call into question the basis of the Swedish model – namely a strong contractual tradition based on powerful social partners who enjoy considerable autonomy from the public authorities – but instead reflected a transition and adjustment of the Swedish model to the new challenges posed by so-called ‘post-industrial society’.

Also during this period, the various reforms of the Swedish social protection system essentially took the form of a temporary reduction of income compensation and, perhaps with the exception of the fundamental restructuring of the pension system, left the architecture of the Swedish welfare state system almost intact. The Swedish social protection system remained, by international standards, clearly universal and inclusive in nature and still enjoyed a high level of across-the-board political and public support. The structural reforms undertaken in the tax and benefit system – in particular, the reshaping of the pension system and the tax reform initiated in the early 1990s aimed at strengthening work incentives and fostering investment in education (human capital) – was also clearly in line with the general philosophy of the original Swedish model favouring the ‘work-first line’, integrative transitions across the life course instead of passive support and social exclusion.

Last but not least, the third main element of the Swedish model – the extensive use of active labour market policy (ALMP); that is, the overall *policy of activation* – still occupied a central role in Swedish stabilisation policy. Its re-orientation towards a supply-oriented policy (occupational and geographical mobility, active search programmes, labour market training and so on) in many respects appears to be in accordance with the strategy initiated in the 1950s.

Since the publication of the article in question, two major events have occurred in Sweden that could cast doubt on our optimistic view of a renaissance of the Swedish model. First, the Social Democratic Party lost power and a conservative-liberal coalition government took office in September 2006. The same political coalition was re-elected at the parliamentary election in September 2010.² During its first term of office, the new government conducted several neoliberal policy reforms, concerning among other things the tax and social protection systems, as well as reforms aimed at opening up public welfare services (health care, elderly care, social services and education) to ‘competition’. Second, in early autumn 2008, the global economic recession hit Sweden severely and some aspects of the macroeconomic policy implemented might also be interpreted as a departure from the original model, in particular regarding its ability to maintain full employment in the long term.

The chapter is structured as follows: after a description of the major policy developments since 2006 and their potential impacts during the 2008 crisis we analyse the policy strategy adopted, and identify the groups particularly affected by the recession. Finally, Section 4 reflects not only on the potential impact of the Great Recession on the Swedish model but also on the role of the social model in the country’s economic recovery.

2. Development of the Swedish model prior to the crisis

The several structural reforms undertaken by the conservative-liberal government during its first term of office (2006–2010) were aimed principally at increasing labour utilisation in the long run, through essentially supply-oriented measures, such as tax cuts and reforms of the social

2. In October 2014 a minority Social Democrats and Greens government was installed.

protection system (unemployment benefit and sickness insurance). Several tax reforms were conducted aimed at reducing the tax wedge and increasing labour supply at both the extensive and intensive margins. The inheritance and wealth taxes were abolished in 2004 and 2007,³ respectively. The corporate tax rate was reduced,⁴ as was the total levy of social security contributions. Reforms of income tax have also been implemented gradually over the past five years. The most important tax reform in this context was the introduction of a system of in-work tax credits aimed at strengthening work incentives for low-income earners and a reduction of marginal tax for high income earners; the two reforms entailed a reduction of marginal tax of around 2–3 percentage points.

Other important structural reforms concern the social protection system, namely unemployment insurance (stricter eligibility rules and lowering of benefits) and sickness insurance (more stringent rules, increased supervision and monitoring of a person's capacity to work). A new *unemployment insurance system* took effect in 2007. Eligibility for unemployment benefits after the reform was based on the past 12 months' earnings instead of the past six months'. The reform also implied a significant diminution in the generosity of the Swedish unemployment insurance system, as the income replacement rate was reduced from 80 per cent to 70 per cent after 200 days of unemployment. Furthermore, the maximum duration for receiving unemployment benefit was reduced to 300 days (450 days for unemployed people with children). The maximum daily benefit was lowered from SEK 730 to SEK 680.⁵ Altogether, this means that the benefit level was decreased by around 3 percentage points.

Furthermore, the right of job seekers to restrict their search during the first 100 days to jobs in line with their formal qualifications and vicinity was abolished. While these structural reforms might have increased 'work incentives' and job search intensity⁶ and might have reduced

3. The abolition of the inheritance and gift tax was initiated and implemented by the former Social Democratic government.

4. From 28 per cent to 26.3 per cent.

5. 1 SEK= 0.11 euro.

6. A study conducted by the National Institute for Economic Research, NIER (2010), shows that the gradual introduction of income tax credits and the various reforms of the social protection system (unemployment and sickness insurance) between 2006 and 2010 decreased the total marginal tax effect by almost 5 percentage points. According to the same study, the so-called threshold effect (that is, the net increase in income due to taking a job) has also increased significantly.

unemployment duration it should be stressed that this reform in itself does not improve the employability of vulnerable groups in the labour market and is also critically dependent on the development of labour demand for these groups. We may also contest that such a reform – in particular the abolition of the right of job seekers to restrict their search to jobs in accordance with their formal qualifications and vicinity – may lead to more efficient resource allocation in the economy, in particular in a period of reduced labour demand.

The second major reform concerns modifications in the financing of the unemployment insurance system: the contributions of the various Unemployment Funds administered by the trade unions were, after this reform, differentiated according to the unemployment level in the sector/industry concerned.⁷ In other words, a system of experience rating was introduced, individual unemployment insurance contributions being raised or lowered depending on whether unemployment increases or decreases in an industry. This reform entailed a large increase in individual contributions: in some cases, individual unemployment insurance fees tripled. The consequence was both a large decrease in union membership and a dramatic decline in the number of dependent employees covered by the unemployment insurance system: around 500,000 employees left the unemployment insurance system between 2007 and 2008.⁸ The most frequent reason for leaving the unemployment insurance funds was financial strain due to the rise in individual fees. The drop in membership was particularly severe in the hotels and restaurants, retail and transport sectors, as well as among municipal workers (see Eliasson 2008). Between 2006 and 2013, union density declined by 11 percentage points for blue-collar workers and by 4 percentage points for white-collar workers⁹ (see Swedish Mediation Office 2012 and Kjellberg 2014).

Obviously, the government's main objective with this reform was to indirectly influence the outcome of wage bargaining by weakening the bar-

7. The Swedish public unemployment insurance system (UI) is voluntary, regulated and subsidised by the state, but is administered by the trade unions' unemployment insurance funds (Ghent system). Formerly the UI membership fee was 10 per cent of the total benefit paid, while 90 per cent was assured by taxes. In the wake of the reform the membership fees cover 40–45 per cent of the UI, entailing an increase in individual fees.

8. The share of the workforce covered by unemployment insurance decreased from 80 per cent to 67 per cent between 2007 and 2009.

9. From 77 to 66 per cent for blue-collar workers and from 77 to 73 per cent for white-collar workers. For wage earners as a whole union density declined by 7 percentage points between 2006 and 2013 (see Kjellberg 2014).

gaining power of trade unions and therefore to induce wage moderation. The modification of the financing of unemployment insurance and the corresponding diminution of the number of persons covered by it meant that a large number of wage-earners – in particular low-paid/low-skilled employees with unstable employment conditions – lacked sufficient protection in case of unemployment, potentially a major problem during the 2008 recession. In other words, there are strong reasons to believe that the recession increased the number of social benefit recipients among individuals not covered by or entitled to unemployment insurance, increased income inequalities (see next section) and amplified the risk of social exclusion for vulnerable groups. On the other hand, the increase of unemployment risk in connection with the global crisis has partly reversed the negative trends in unemployment insurance fund membership and also in union density. It should also be stressed that, despite the decline of union membership, Swedish union density remains high by international standards (70 per cent) and the coverage rate of collective bargaining is still around 90 per cent.¹⁰ In this sense it can be said that the Swedish model of industrial relations to date has been only marginally affected by these reforms, implying that the bulk of labour market regulations, working conditions and wage setting in Sweden will continue to be determined and regulated by collective agreements.

The Swedish model has been based on a strong political commitment to the goal of full employment. Despite the current political rhetoric, we argue that the policy developments testify to a weakening of this commitment with a clear reorientation of macroeconomic policy towards price stability and budget balance. Employment rates are still clearly below their early 1990s level and unemployment rates are also significantly above the rates prevailing during the 1970s–1980s. True, the decline of employment rates since the early 1990s also reflects major investments in education and a general trend toward a postponement of entry into the labour market. However, compared with other EU member states, such as Austria and Germany, the transition from school to work remains to some extent problematic in Sweden, with comparatively high youth unemployment. If Sweden might be classified as ‘no country for young men/women’ (to invert Yeats), on the other hand it is a relatively good country for old men (women), with the highest employment rates among senior workers in the EU.

10. The coverage rate of collective agreements is around 85 per cent in the private sector and 100 per cent in the public sector.

3. Impact of the crisis on the Swedish economy and model

In the wake of the global financial crisis, the Swedish economy started to deteriorate rapidly in the second half of 2008. In 2009, Sweden's GDP decreased by 5.1 per cent, the worst deterioration since the Second World War. With the severe drop in output and aggregate demand, employment declined sharply. Between 2007 and 2009, employment decreased by more than 100,000, while the unemployment rate increased from 6.2 per cent to 8.4 per cent. The fall in output and employment was particularly marked in manufacturing, with decreases of 25 and 20 per cent, respectively, while employment increased by almost 10 per cent in the private service sector and in construction. With regard to Swedish manufacturing, the fall in employment was particularly marked in export-oriented industries. Due to the sharp increase in unemployment, local plant closures and the overall reduction of economic growth, the recession led to a reduction in tax revenues for local authorities, which are responsible for the provision of social services, health care and education. In a first phase, this situation led to severe budget cuts at the local level and a decline in public employment, mainly among public employees on short-term contracts.

3.1 Policy responses: macroeconomic and labour market policy

In the face of the drastic worsening of the economic situation, as well as the growing awareness that Sweden will experience a much more dramatic drop in output and employment, the government implemented financial and fiscal stimuli measures at the end of 2008. In particular, extensive investments in the maintenance and operation of the road and rail networks were decided on. In response to the crisis of the financial system the government launched a guarantee programme, aimed at securing the medium-term borrowing of banks and mortgage institutions and lowering the cost of borrowing for households and companies. In order to stimulate activity and maintain labour demand in the construction sector, work in the form of repairs, maintenance and improvement of one-family houses and tenant housing were made tax deductible. During 2009–2010, the government announced further counter-cyclical expansionary fiscal measures to combat the crisis. These new fiscal measures were focused on two areas in particular: increased government grants to municipalities and county councils and more resources for active labour

market policy. In September 2009, the government decided on a further increase of SEK 10 billion in the central government grant to municipalities and county councils in 2010, as well as further investment in infrastructure (SEK 1 billion) in order to maintain and secure employment in the public sector.

As far as tax policy is concerned, the government introduced a fourth step in the abovementioned in-work tax credit (SEK 10 billion), a reduction in social security contributions for the self-employed, a further reduction in income taxes for low income pensioners and an increase in housing benefit for the long-term sick and the long-term unemployed. In order to limit the negative impact on poverty and social exclusion of the 2007 unemployment insurance reform in July 2009 the government decided on a reduction in individual unemployment contributions. The government also amended membership requirements temporarily so that members of an unemployment insurance fund in 2009 would be able to count one month extra for each month of membership in 2009.

Since the late 1950s, active labour market policy (ALMP) has played a vital role in Swedish stabilisation policies. The preference for the principle of employment promotion (work-first principle) has always predominated over benefit options for the unemployed. In contrast to the 1990s crisis, when the bulk of counter-cyclical measures essentially took the form of an increase in the number of participants in various active labour market policy programmes, the Swedish government relied to a greater extent on expansionary fiscal and monetary policy to counteract the current economic recession. It is also clear that, in comparison with the 1990s crisis, the room for manoeuvre in which to conduct a more expansive macroeconomic policy was greater than previously, due to healthier public finances at the start of the economic downturn. Regarding active labour market policy measures, the volume of participants in the various ALMP programmes was gradually increased, but never attained the number of participants enrolled during the last severe recession in the early 1990s. The difference concerns not only the number of participants, but also the composition of ALMP measures. Compared with the previous crisis, the current government focused more on labour supply-oriented and matching measures (job search assistance, coaching) and/or work experience and trainee schemes. The number of participants in traditional labour market training has also slightly increased, but much less than in the previous recession. All in all, the number of participants in labour market policy programmes has increased but,

as already mentioned, less than during the previous economic crisis. It should also be noted that public sector job creation has not been used in connection with the crisis, but the increase of central government grants to local governments has certainly had an effect in limiting the fall of employment in the female-dominated public sector.

3.2 Changes in employment

Traditionally and in line with the core elements of the Swedish model, economic downturns and structural changes have seldom been accompanied by measures aimed at maintaining the level of employment. In contrast to other European member states, such as France or Germany, public policies aimed at reducing working time (work sharing) or facilitating temporary layoffs have not been favoured in Sweden. In the early phase of the recession, employment adjustments therefore essentially took the form of external numerical flexibility, in particular a large reduction in the number of agency workers and temporary contracts. The employment decline was also particularly dramatic among low educated and low skilled workers, while employment among employees with a high level of education was only slightly affected (employment even increased between 2007 and 2009 among high skilled employees).

As far as gender is concerned, the relatively stronger impact of the crisis on male unemployment is related to the abovementioned decline of employment in the male-dominated export-oriented manufacturing sector, but compared with the previous crisis (1993), the gender gap in unemployment has remained much lower. There are strong reasons to believe that this is related to the more rapid decline in employment in the public sector at the local and regional levels in the initial phase of the crisis. However, in a second phase, the additional appropriations to local government by the Swedish government helped to limit the decline of public employment and in 2011 public employment was at the same level as in the mid-2000s. The bulk of the adjustment in the public sector took the form of wage moderation and not a permanent decline of public employment. Regarding older workers, Swedish companies seem to have used early retirement to accommodate the recession much less than in previous economic downturns. The employment rate of senior workers (55–64 years of age) has, to date, remained almost unchanged, while the unemployment rate increased only slightly, from 3.2 per cent in 2008 to 5.2 per cent in 2009.

Youth unemployment, however, as well as unemployment among non-natives, has been more sensitive to fluctuations in the business cycle and the employment prospects of young people and foreign-born people have worsened significantly since the end of 2008. In the second quarter of 2009, youth unemployment rates reached 29 per cent and those of foreign-born people 16.3 per cent (compared with 7.9 per cent for natives). Despite a decline after 2009, youth and foreign-born unemployment rates remain clearly above their pre-crisis level.¹¹

The dramatic increase in youth unemployment during the crisis might be ascribed to several factors: first, a significant increase in the youth labour supply, in other words, a relatively larger cohort of young people entering the labour market when the recession started; second, the incidence of temporary contracts is higher among young people; and third, the Swedish Employment Protection Act, more specifically, the application of the seniority principle (last in, first out) favours workers with long seniority in the redundancy process.¹² While the labour supply of people with an immigrant background was unchanged, the increase of unemployment among non-natives is also related to their weaker attachment in the Swedish labour market (higher incidence of temporary contracts, lower work experience and concentration in the low skilled segment of manufacturing industry and the service sector).

The causes of the riots that took place in some Stockholm suburbs with large immigrant populations in May 2013 cannot be reduced to economic factors, policy failure or the growing difficulties that some groups immigrants face in trying to enter the Swedish labour market. The riots were the outcome of a broad set of complex and interrelated social, cultural and structural factors. During the past three decades several elements might explain the growing difficulties of some groups of immigrants in trying to obtain a foothold in the Swedish labour market, not least the change in the composition of the immigrant population (entailing

11. Youth unemployment was 23.6 per cent in 2013 compared with 19.0 per cent in 2007; for non-natives the unemployment rate was 16.3 per cent in 2013 compared with 12.1 per cent in 2007 (Statistics Sweden 2014).

12. It should be noted, however, that the order of priority may be modified by collective agreement but case law indicates that there are limits to bargaining freedom in this respect: a collectively agreed redundancy list may not be contrary to good practice or otherwise improper. Under an amendment in the Employment Protection Act introduced in 2001, in the interests of retaining necessary skills in small businesses, employers (maximum 10 employees) may exempt from the procedure of selection for redundancy a maximum of two employees who are particularly important to the company.

a greater number of political refugees and family reunifications) and in the distribution of employment and skills structure related to the development of a knowledge service economy. Alongside these factors, which in my view are determinant, the rise of income inequalities, the increasing housing segregation (ethnic enclaves) and the persistence of discrimination during the past two decades also might explain growing perceptions and feelings of social exclusion in some urban areas, leading to anti-social behaviour. But the difficulties experienced by Swedish society in trying to integrate some ethnic groups into the labour market and the recent unrest in some Swedish suburbs cannot be used, as some commentators have tried to do in the media, to call into question the effectiveness of Sweden's generous and long-standing integration policy and the targeted measures directed towards vulnerable groups. On the contrary, the unrest shows that additional educational and active labour market policy measures have to be implemented in order to further limit early drop-out from the education system, improve the educational and skill level of recently arrived immigrants and to further fight against discrimination in the labour and housing market.

3.3 Collective bargaining, wage setting and income inequalities

Most labour market regulations, working conditions and wage setting in Sweden are determined and regulated by collective agreements, and an analysis of measures initiated to combat the impact of the economic crisis on employment cannot be limited to government action.

As previously mentioned, no government measures for maintaining employment by means of short-time working were implemented in Sweden. The initiatives came instead from the two sides of industry. If the employment adjustments in Sweden mainly took the form of external numerical flexibility, the severity of the recession, the fear that the number of dismissals will further increase and the fact that the crisis was principally demand-driven led the trade union federation IF Metall and the Association of Swedish Engineering Industries to conclude a framework agreement on temporary layoffs and wage adjustments in March 2009. Under the agreement, an employee temporarily laid off from work received at least 80 per cent of their usual monthly wage.¹³ Some 400

13. On average, these short-time working agreements entailed a 18 per cent reduction in working hours and a 13 per cent reduction in wages..

companies affiliated to the Association of Swedish Engineering Industries concluded such agreements and according to IF Metall these agreements helped to safeguard between 12,000 and 15,000 jobs.

As far as wage setting and wage development are concerned, experience from the deep economic crisis of the early 1990s shows that wage moderation characterised wage developments during the second half of the 1990s and early 2000s. There were therefore strong reasons to expect that, in the wake of the current severe economic and financial crisis, wage agreements would also be concluded to preserve employment stability and limit further increases in unemployment. The outcome of the 2009–2011 bargaining round indicates that wage moderation has prevailed in Sweden. The resulting slowdown in the rate of increase in labour costs, combined with the depreciation of the Swedish currency related to the expansionary monetary policy conducted by the Swedish Central Bank, helped to alleviate the negative effects of the recession on output and employment and partly explain the increase in exports during the 2010 recovery.

Looking now at the development of the earnings distribution, the dispersion of disposable income has also increased in Sweden in the long run. Although Sweden belongs to the set of countries with the lowest earnings inequalities, the Gini coefficient increased by 26 per cent between 1991 and 2008, although it fell slightly between 2007 and 2009. During the current recession the reduction in disposable income has been particularly marked at the two ends of the income distribution. Low and high earners both experienced a significant decline in disposable income between 2007 and 2009. Among high earners, the decline of income might be ascribed principally to the fall in capital income related to the global financial crisis. There are good reasons to believe that the deterioration among low earners might be ascribed to the conjunction of several factors: rising unemployment, particularly among low skilled and low paid workers; the dramatic increase in youth unemployment (new entrants into the labour market not covered by the unemployment insurance system); and the abovementioned unemployment insurance reform initiated in 2007. Although the government, as already mentioned, changed the qualification rules in 2009 and introduced a ceiling on individual contributions, there is reason to believe that a significant part of the decline in average disposable income in the first decile was a consequence of this reform.

4. Lessons and prospects five years after the Great Recession

In an international perspective, Sweden seems to have managed to overcome the current economic crisis better than many other member states. In spite of a long-term tendency to reduce the de-commodification of its welfare state, Sweden, with its large, encompassing and generous social protection system still possesses relatively robust automatic stabilizers. There are strong reasons to believe that a dramatic fall in GDP might have quite different implications for household living standards in countries with weak automatic stabilisers and/or constrained public finances, in other words, with limited room to manoeuvre to conduct a counter-cyclical macroeconomic policy. Without doubt, the generous and encompassing Swedish social protection system has helped to ameliorate the consequences of the crisis for individuals (limited impact on income and inequality), while the benefit and transfer systems played their role of shock absorber and economic automatic stabiliser. The recent improvement in the Swedish economy might also be ascribed to the strong expansionary fiscal and monetary policies.¹⁴ Compared with previous economic downturns, Swedish economic growth over recent years has been driven less by increases in exports than by an increase in public and private consumption, due both to increases in disposable household income¹⁵ and the additional appropriations to local government decided on in 2009 and 2010.

As stressed previously, due to healthier public finances at the start of the economic downturn the room for manoeuvre for conducting a more expansionary macroeconomic policy was greater than during the previous recession (1993). Overall, the Swedish experience shows that strong public finances are essential for handling the challenges confronting fiscal policy, especially in a deep recession. While Swedish public finances have been somewhat weakened, deficits have also been limited. Against this background and in light of the recent economic recovery the needs of fiscal consolidation and excessive deficit procedure will remain limited,

14. Already in 2010, the Swedish economy was in strong recovery with rapid growth (6.6 per cent in 2010, 3.7 per cent in 2011), increasing employment and declining unemployment.

15. The increase in disposable income can be ascribed to the cuts in income tax and also the increase in some transfers, such as housing benefit for low earners or child allowance. Comparing the trends in real GDP and real gross household disposable income (HDI), it appears clear that Sweden, during the period 2007–2009, experienced an increase of HDI (+5.1 per cent) despite the dramatic fall in output (–5.1 per cent in 2009).

which implies that the negative impact of restrictive fiscal policy on employment in the public sector will also be limited in Sweden compared with other EU member states.

All in all, previous developments tend to show that political change and economic and structural reforms have to date only marginally modified the core components of the Swedish model. The structural reforms of the tax and benefit systems aimed at strengthening work incentives are still clearly in line with the general philosophy of the original Swedish model favouring the 'work-first line' instead of passive support. Even if the volume of participants in ALMP programmes was lower during the current recession overall the policy of activation still plays a major role in Swedish stabilisation policy. Last but not least and despite the above-described decline of union density, the two sides of industry remain the two main actors regarding both labour market regulations and wage setting: the bargaining system remains centralised and coordinated. In contrast to countries with weaker industrial relations systems and unbalanced bargaining power between the two sides of industry, the nature of the Swedish industrial relations system has also entailed a more balanced sharing of the cost of the crisis. The Swedish institutional set-up also explains why Sweden still has one of the highest levels of job quality and why the current recession has not adversely affected working conditions by means of wage cuts, longer working hours, higher workloads and increased work intensity, as it has in other EU member states (see Anxo 2011).

The Swedish experience is therefore a good illustration of the positive role played by both healthy public finances and a strong social safety net in mitigating and absorbing the negative impact of external macroeconomic shocks. More broadly, the Swedish experience during the last recession illustrates the resilience and long-term viability of a societal model based on a universal and generous social protection system,¹⁶ egalitarianism, pro-active policies for promoting gender equality and fighting against discrimination and social exclusion, a developed social dialogue as a mechanism for regulating the labour market and social policies, and strong public and political involvement in the provision of

16. It should be stressed that, besides a high level of employment, a prerequisite for securing the long-term sustainability of such a generous social protection system is a tax system that guarantees adequate public revenue. In this regard it should be recalled that the Swedish tax burden remains among the highest in Europe, despite falling somewhat during the past decade.

a wide range of public services. The ‘Swedish success story’ during the last recession cannot therefore be reduced to early fiscal consolidation measures. It is clear that both the automatic stabilisers embedded in the Swedish societal model, the additional government support (Keynesian counter-cyclical measures) and the social dialogue have had an important effect in mitigating the negative effect of the crisis on employment, welfare and social exclusion.

Although the reforms undertaken by the previous government have only marginally affected the Swedish model and its macroeconomic policy has helped to absorb and limit the negative impacts of the crisis on employment and income inequalities in the short run, we cannot rule out that the long-term consequences of the crisis might be significant. Despite the abovementioned signs of recovery and a rising employment trend, the overall unemployment rate remains high, at 8.1 per cent (average 2013), a level much higher than in previous periods (1960–1991), when unemployment rates oscillated between 2 and 3 per cent. The long-term consequences of high youth unemployment and the deterioration of the labour market for people with an immigrant background also remain worrying. As shown by previous empirical evidence (see Nordström-Skans 2004) the potential scarring effects of an early period of unemployment may have a long-lasting negative influence on subsequent employment performance and income development across the life course. Furthermore, an early period of unemployment may affect the timing of other critical transitions and events, such as the transition from school to work and the constitution of an independent household, as well as access to housing, parenthood and fertility patterns, career opportunities and wage development (see Anxo *et al.* 2010). Some recent empirical evidence (see Anxo 2011 and 2013) tends also to show that we may not rule out either that the current crisis, like the deep recession of the early 1990s, will mean that, in future, a growing share of Swedish companies will rely increasingly on external numerical flexibility, with a rise in the use of short-term contracts and agency workers. If this is the case, this development may worsen the duality in the labour market between insiders and outsiders, alter the conditions of entry into the labour market and delay the acquisition of a permanent and stable job. It is also clear that if Sweden fails to re-establish the conditions for a return to full employment, in particular to reduce unemployment and increase employment rates for some of the abovementioned vulnerable groups, we cannot exclude a progressive decline of the Swedish model, its coherence and the robustness of its social cohesion.

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Between crisis corporatism and revitalisation: trade union policy in the era of European financial market capitalism

Hans-Jürgen Urban

1. Introduction: return of the state and the trade unions

States and trade unions play a key role in the European employment model. In terms of their capabilities, however, neither have been in particularly good shape for some time. There has been a broad consensus in the literature that the pressure for change to which they were subjected in the course of the transition to deregulated financial market capitalism forced both onto the defensive. This applies both to welfare states (see Bosch, Rubery and Lehndorff 2007a and b; Pierson 2001) and to trade unions (see Brinkmann *et al.* 2008; Dörre 2010).

When crisis struck global financial market capitalism, however, both the state and the trade unions appeared to make a political comeback. Many states demonstrated unanticipated capabilities. Economic stimulus packages, encroachments on capitalist property rights and measures to restructure the financial sector were just some elements of a new state interventionism practiced by governments across the political spectrum (Hassel and Lütz 2010; Mayntz 2010). At the same time, social dialogue gained in importance within the framework of state crisis policies (Glassner and Keune 2010a and b; Hyman 2010a). In some countries cuts in working time, wage moderation measures and flexibilisation of remuneration contracts were agreed backed by statutory provisions and state compensation payments. This negotiated response to the crisis made it possible to ensure that companies remained in business and employment was secured. In the political arena amenable trade unions often encountered cooperative government policies (Hyman and Gumbrell-McCormick 2010a). On occasion the trade unions were able to play an influential role in these social pacts. This was the case in Germany, for example, whose crisis-policy model is the focus of this chapter. The German trade unions were a decisive factor in the 'German labour market

miracle' (Möller 2010), which made it possible to stabilise jobs, enterprises and value creation in the industrial sector, although the slump in production and orders was particularly sharp. This success prompted a debate on a possible trade union renaissance, giving rise to new academic interest (see the special issue of *Industrielle Beziehungen* 4/2012) and to new recognition among functional elites (Urban 2010a).

Underpinned by a new strand in international trade union research and by observations of developments in Germany we shall argue that although corporatist arrangements, as elements of a national crisis corporatism, entailed high costs, they proved effective for trade unions that had become rather short on political muscle. It may be doubted, however, that the new social pacts represent an appropriate institutional framework for future interest representation and a sustainable organisational revitalisation of the trade unions. For the trade unions a strategy of autonomous revitalisation would appear to be more promising, although to be sure this entails a revival of trade union power resources and a strengthening of trade union negotiating and organisational capabilities.

The chapter is structured as follows. A brief outline of the power resource approach in revitalisation research (Section 2) is followed by a presentation of the German social pact and an attempt to formulate a number of generalisations based on the thesis of the new crisis corporatism (Section 3). Complementing these considerations we outline examples of successful trade union revitalisation, which, with reference to IG Metall, lead us to posit the notion of successful organisational learning (Section 4). After noting the requirements and limitations entailed by the emerging regime of precarious authority in Europe, we discuss a number of conclusions for trade union practice and touch on some open research and strategic issues.

2. Power resources and trade union revitalisation: theoretical context

Trade union research in Germany has concentrated mainly on spelling out the crisis dimensions of the trade union situation; there has been less attention to the options and requirements of trade union recovery. Gradually, however, a new strand of international trade union research, known as the 'strategic unionism approach', has emerged, which has become a branch of research in its own right in the form of 'labour re-

vitalisation studies (Voss and Shareman 2000; Frege and Kelly 2004; Huzzard, Gregory and Scott 2004; Dörre 2008; Gall 2009; Haipeter and Dörre 2011; Gumbrell-McCormick and Hyman 2013; Schmalz and Dörre 2013). According to this new approach even under financial market capitalism the trade unions find themselves in an open, undetermined situation. Rather the economic, social and political/cultural contexts articulate a realm of possibilities with a diversified opportunity structure. This makes a range of strategic options available to the trade unions, which vary in terms of their potential with regard to the envisaged revitalisation (Huzzard 2004). In the words of Hyman and Gumbrell-McCormick (2010b: 327), 'Hard times can often result in strategic paralysis, but can also be a stimulus for the framing of new objectives, levels of intervention and forms of action'. Successful selection of strategic options and viable engagement in innovative practices, however, require a realistic assessment of the context for action, action strategies adequate to meet the challenge and sufficient implementation capacity ('strategic choice', see also Child 1997).

Whether the available options can be exercised, however, depends not least on power. Power can here be understood to mean the capacity of individuals and organisations to realise class interests. One can distinguish here – with reference to E.O. Wright (2000) – between structural and associational power. The former arises from the position of wage earners in the labour market ('labour market power') and within the production process ('production power'). Associational power, by contrast, arises when wage earners form collective organisations, in terms of which the trade unions are the key actors in political interest representation. In the course of the debate institutional power introduces a further dimension of trade union power (Dörre 2009). This is based on trade unions' position within the institutional arrangements of the welfare state. It is also determined by the social balance of power between the state, capital and labour, which tends to remain stable despite brief cyclical fluctuations. A fourth dimension, finally, is the communicative power of trade unions, which might be termed trade union 'soft power'. This comprises the ability to intervene successfully in hegemonically pre-structured public spheres. Communicative power is discernible in the conflict concerning 'opinion-making' and the ability to obtain societal recognition of one's interests (Urban 2010b: 444).¹

1. For further development of the power resources approach see the contributions in Schmalz and Dörre (2013).

3. Trade union interest representation and the crisis of European financial market capitalism

In the transition to deregulated financial market capitalism the trade unions lost power in every dimension (Addison and Schnabel 2003; Brinkmann 2008; Dörre 2010; Urban 2010b, 2013a and b). Even though developments in individual countries varied depending on the politico-economic and institutional contexts, overall the trade unions were weakened by the great crisis.

3.1 A success model and its costs – the case of Germany

Germany was no exception, but the German variant of negotiated response to the crisis is held up as a success story. In essence, it involves the involvement of the trade unions in a state crisis strategy to stabilise industrial employment and value creation, but oriented towards easing enterprises' financial burden and largely refraining from imposing the costs of the crisis on financial market actors. What the state offered the trade unions initially came as something of a surprise because it came from a conservative-led government coalition. The Agenda 2010 policy of a previous Social Democrat-led government and its at times aggressive policy of confrontation with the trade unions appeared to confirm the thesis of a 'disengagement' between the trade unions and the Social Democrats (Piazza 2001) and the end of German corporatism. However, even before the Bundestag election of 2009 the Grand Coalition was making political overtures to the trade unions. A new *inverse lobbying* was discernible. While in traditional lobbying social organisations seek to pursue the interests of their clientele by influencing state decision-making, in inverse lobbying the main stream of intended influence flows in the other direction. The initiative was taken by the political parties or government representatives. Such a strategy seemed at first sight to be more attractive to party and government representatives of the SPD. The termination of the 'special relationship' between the trade unions and Social Democrats had not done them any good at all, as disastrous opinion polls and election results prove. However, under Chancellor Angela Merkel evidently the 'social democratisation' of the CDU/CSU and its repositioning towards the centre went hand in hand with a corporatist revival. As a result, the trade unions re-emerged as a potential resource in support of CDU/CSU policy strategies and stabilising political majorities (a 'vote seeker' function). Under pressure of the crisis and the

conflict potential of the adopted crisis policy inverse lobbying recommended itself as the core of a cross-party tripartite social pact.

It is no easy matter to determine the outcome of the German response to the crisis from a trade union standpoint. On the plus side, one might mention the success in securing employment and the enhanced public esteem for trade unions. Even among critics of corporatism trade union leaders and policies in the tripartite negotiating rounds were acknowledged. 'They proved themselves as crisis managers and in the course of political horse-trading won concessions (generous rules on short-time working, scrappage premiums) and outcomes (securing core workforces) that were not achieved in other countries even with militant protests' (Dörre 2011: 268; also Gumbrell-McCormick and Hyman 2013). Clearly, the new social pact, made necessary by the crisis, opened up new channels of influence to the trade unions, which they were able to use in pursuit of their interests (Urban 2010a and 2013). However, it came at a price. For example, securing jobs by cutting working time entailed a reduction in temporary jobs and considerable concessions on the part of the core workforce with regard to wages, performance and working conditions. Besides relatively low nominal collectively agreed wage increases the tendency was for collective bargaining periods to increase and for agreed wage increases to be delayed. Lump-sums and one-off payments also increased, moderating future wage increases (Bispinck 2011). At the same time, employment security was linked to accelerated enterprise restructuring, leading to far-reaching performance intensification and an adverse impact on workers' health (Schröder and Urban 2011). Furthermore, this policy model did not prove amenable to realising some of the essential aspects of the trade union strategy for tackling the crisis. This includes IG Metall's demand for a public equity fund, to be based on a levy on private wealth and to be used as an instrument of crisis-policy intervention in the system of property ownership and the necessary structural change (Urban 2009). This was not feasible, however.

Looking at the German social pact from a power-resource perspective it is clear why the trade unions had to pay a high price to secure employment and why more far-reaching trade union demands were not achievable. Corporatist negotiation systems are based on the principle of political exchange (Hassel 2009: 9–10). Thus success is generally not possible without concessions. As a consequence, the inherent logic of negotiation operates as a demand filter, which winnows out the demands of a corporatist actor that conflict too sharply the interests of the others.

Which set of interests and demands ultimately prevails depends, to be sure, on the negotiating skills and institutional rules of the exchange, but above all on the endowment of negotiating clout. The German social pact, too, follows this logic. Thus workforce retention – for example, by means of short-time working – and maintenance of industrial value creation (for example, by means of the ‘scrappage premium’) were in the interests of the trade unions and the employers’ organisations, as well as a government concerned about popular support. These aims were thus capable of gaining a consensus and implementable, forming the basis for ‘discourse and decision-making coalitions’ encompassing a range of actors (Hegelich 2010) who paved the way for these demands, in the general interest. The situation was different with regard to the demand for a public equity fund. This was not in the interests of all the relevant actors and thus agreement could not be reached. The public equity fund would have represented a structural intervention in the crisis conflicting with the rules of the economic mainstream. This was considered indispensable by the trade unions and some sections of the general public, but clearly was anathema to the asset and power interests of the capital organisations and an economic-liberal government pursuing its own brand of *Ordnungspolitik* (in a 2012 speech German finance minister Wolfgang Schäuble defined *Ordnungspolitik* as ‘economic and fiscal policies that are consistent with the principles of markets and competition’). This proposal thus didn’t even make it onto the agenda of the negotiation rounds.

3.2 A new crisis corporatism?

The German social pact thus brought the trade unions considerable defensive successes, but also substantial costs, while some of their more far-reaching demands were thwarted. However, it was not only in Germany that negotiated solutions to the crisis and a new dynamic of wage and working-time moderation prevailed (see, for example, Hyman 2010; Glassner and Keune 2010a and b). This revival of social partnership and social pacts can also be understood as a further stage in the metamorphosis of the classic corporatism of the social democratic/Keynesian period (Schmitter and Grote 1997; Traxler 2004; and for a critical view, Hassel 2009: 13).

In the latest research particular attention is paid to the significance of the power resources and interests of the state, trade unions and organisations representing the interests of capital, on the basis of which

Table 1 Variants of corporatism

	Social corporatism	Competitive corporatism	Crisis corporatism
Periods in financial capitalism	Preliminary period	Development period	Crisis period
Power endowment of actor constellations	Alliance of the strong: Trade unions: strong; capital: strong; state: strong.	Asymmetrical alliance: Trade unions: weakened; state: weakened; capital: strong.	Alliance of the weak: Champion: Financial capital; trade unions: weak; state: weakened; real capital: weakened.
Distribution regime	Symmetrical (classes) distribution compromise between labour / capital/state	Tendency towards asymmetrical distribution in favour of capital and at the expense of labour and the state	Structural-asymmetrical distribution in favour of financial capital and at the expense of labour, the state and real capital
Normative model	Redistribution/solidarity	Competition/solidarity	Social pacts as communities of acute need
State type	Welfare state	Competition or market state	Crisis state
Trade union type	Distribution/actor	Competition/partner	Crisis/facilitator

Source: Author's presentation.

corporate actors define their strategic preferences (Boccardo 2008; Hassel 2009). The macroeconomic aspect is particularly highlighted in this context. Analysis was improved by distinguishing between 'policy interests' and 'power interests'. Both can be given different strategic weight (Hassel 2009: 9–13). While policy interests give rise to strategies oriented towards the solution of political problems or the achievement of political goals, power interests primarily promote strategies for stabilising a government's political power or the organisational power of associations. From the standpoint of the state it has an interest in cooperating with the trade unions if the inclusion of the latter can help to solve important economic or social problems; or if the trade unions can and wish to help to obtain public acceptance of government actions or increase their electoral chances. A strategic interest in social pacts on the part of trade unions arises when trade union capacities extend to mobilising some sort of veto or blockade against the government, but not to obtaining higher wages, secure employment and generous social transfers via confrontation. Also relevant is whether representing members' interests in social pacts can contribute to trade union stability. In this context

actors' interests and strategic preferences, and thus also stability and the durability of cooperative alliances, can change rapidly

Empirical research on social pacts has revealed striking differences between *Länder* in the formation of corporatist arrangements before the crisis, but also similarities. The similarities were relatively independent of institutional contexts and political traditions. The description of these competitive-corporatist alliances as 'coalitions of the weak and the moderate' refers to the actors' endowments of power and strategic calculations (on this see Boccaro and Lim 2006; Baccaro 2008). Weakened governments that, due to globalisation, the electoral system or powerful veto players are unable to solve problems alone come together with trade unions that have lost negotiating clout due to falling membership and general changes in the economy and politics, but which nevertheless retain a certain capacity to mobilise and thus a veto power. Trade union decisions in favour of participation in social pacts were often preceded by considerable internal struggle, in which 'moderates' won out over 'radicals' and took over the strategic direction of the organisation. The employers' organisations' willingness to engage depended on their expectations with regard to the outcome of the social pacts and sometimes proved important not for the coming into being but definitely for the stability of such pacts.

The crisis of financial market capitalism has generated a new macroeconomic context that shapes the actors' interests and viability. This applies, on one hand, to the economy, in view of the sheer scale of the fall in capacity utilisation and production. But it also applies to the state. The new state intervention exhibits a number of substantial differences in comparison with that of the welfare-state era. Nationalisation, economic stimulus and market-correcting regulation took place under the coercion of a severe financial and economic crisis and served the primary purpose of stabilising the country as a financial centre and business location. At the same time, the relevant objectives could be achieved only by means of intense cooperation between nation-states, which in turn limited the capabilities of individual states (Hassel and Lütz 2010). Finally, these ad hoc interventions, which sought to stabilise the economy and the financial system by means of extensive spending programmes and compensation for losses due to private debt, put considerable strain on the state's financial capacities. As a result of the 'biggest rise in debt in peace time' (Wagschal and Jäkel 2010) caused by the crisis most governments not only violated the deficit and debt guidelines of the European Growth and Stability Pact (Streeck 2013: 141–224), but also heightened

polarisation between the euro-states: while countries such as Germany were able to reduce their interest burden because of falling interest rates with regard to the refinancing of public debt, thereby provoking a beneficent response from the financial markets (Bundesbank 2013: 47–67) the public budgets of other countries staggered under the additional weight imposed by exorbitant interest rises.

These particular features suggest that state crisis policy based on cooperation with the trade unions was not merely a warmed up version of pre-crisis competitive corporatism. We shall call the arrangements that emerged from this new constellation ‘crisis corporatism’. In Germany the new corporatism, while certainly in the corporatist tradition, differs somewhat from previous incarnations (see Table 1). The *social corporatism* of Fordist capitalism functioned on the basis of more or less equal actors who resorted to negotiating symmetrical class compromises in the event of conflict. The interests of all the relevant actors had to be acknowledged. The state acted as market-correcting welfare state and the trade unions were the distribution agents of wage earners. The redistribution of market-mediated income streams was largely recognised as a necessary requirement of solidarity. The subsequent *competitive corporatism* developed during a period in which the Fordist welfare state model of capitalism had come under pressure to change, both internal and external. The transnationalisation of the economy expanded companies’ range of strategic options to include relocation and thus strengthened their negotiating clout in relation to both states and trade unions. The interest of wage earners in redistribution became increasingly subordinated to the competitive interest of companies. The state, whose hand had been weakened with regard to the economy, switched focus from a demand-oriented redistribution policy to a competition-oriented supply-side policy (the ‘market state’). For companies, boosting competitiveness takes priority over redistribution, which means that the interest of the workforce in distribution can be satisfied only within the framework of additional competitive gains. This new ‘competitive solidarity’ (Streeck 2000) also subordinated workplace and trade union interest representation, which was not to deny their contribution to company survival in a situation of tougher international competition.

The tripartite alliance that emerged in Germany during the crisis differs significantly from both social corporatism and competitive corporatism. It is plausible to call it a new ‘crisis corporatism’. First, the acute crisis

of financial market capitalism represents a specific macroeconomic context, which differs fundamentally from the period of prosperity and has changed the interests and power resources of corporatist actors. The state, the trade unions and companies in the real economy have come together under pressure from the crisis shock to defend themselves against the mechanisms of the financial markets and the lobbying power of their key actors. Crisis corporatism represents an *alliance of the weak* who consider enterprise and political social pacts as emergency alliances in response to the crisis. This has shaped the policy outcome. Although at the height of the crisis the employment interests of the core workforce were defended relatively successfully a willingness to lay off non-core employees – especially temporary workers – concessions on pay, working time and working conditions by the core workers and the refusal by financial market actors to bear their share of the costs of the crisis make it clear that the distribution interests of wage earners in this alliance remain largely subordinate. Although – as usual – the aggregate wage share briefly increased at the height of the crisis and thus the relative distributional position of wage earners, this development does not reflect any gain in distributional power on the part of the trade unions, but rather a rapid decline in profits in the real economy due to the crisis. Even though this development was reversed as early as 2010, companies in the real economy were not the main beneficiaries, in contrast to the arrangements of competitive corporatism. Rather the dominant crisis policy was accompanied by a value creation transfer from the real economy to the financial economy, resulting in a slump in industrial profits and an explosion of public debt. Government policy was not oriented towards the goal of sustainable improvement of competitiveness but towards the ad hoc stabilisation of companies and as much as possible avoided any regulation of the financial economy. The trade unions and works councils acted as facilitators in companies' urgent fight for survival, which participants and the public alike perceived as emergency alliances in an intensified crisis situation.

4. Stabilisation by professionalisation? Attempts to revitalise power politics

As things stand at the moment we can say that, although the costs and restrictions characterising the inclusion of the trade unions in crisis corporatism cannot be underestimated when drawing up a balance of trade union crisis policy the crisis social pact also furnished the trade

unions with channels of influence that they were in a position to use even with the level of organisational and lobbying clout they currently possess. Whether a rejection of corporatism and a strategy of confrontation would have brought the emaciated trade unions higher dividends is doubtful, especially if one compares developments in other countries. As recent research shows, even before the crisis trade union militancy and political strikes were not always part and parcel of a trade union campaign, but rather a reaction to governments' refusal to cooperate (Kelly, Hamann and Johnston 2013). Even in the crisis – not least because of the trade unions' inadequate power resources – the 'limits of radicalism' were evident (Gumbrell-McCormick and Hyman 2013: 77).

Nevertheless, the manifest limits of militant conflict strategies on the part of weakened trade unions should not lead us to underestimate their organisational power and readiness or willingness to engage in conflict. Interpreting trade union participation in the social pact as evidence of weakness and helplessness is a misunderstanding of the logic of corporatist negotiations. Even under the conditions of such a severe capitalist crisis the inclusion of trade unions in corporatist alliances requires a minimum level of mobilising and negotiating power. Weakened trade unions without veto power are not included, but marginalised, as developments in a number of neighbouring countries show (see Lehdorff on trade unions in this volume). Ultimately, we can conclude, any decision on whether to pursue a cooperative or a conflictual strategy depends on an adequate level of organisational power. In its absence neither have good prospects. This points to the centrality of organisational and negotiating power as a condition of strategic decision-making.

4.1 Systematic recruitment and retention

This realisation seems evident among trade union strategy-makers. After a period of eroding trade union power IG Metall, for example, has been able, both during and since the crisis, to stabilise and expand its power resources.

The first strategic element of this revitalisation strategy involves systematically upgrading recruitment and retention of members in trade union practice. As a result of the crisis in 2009/2010 employment fell in the metal and electrical industry as production slumped. This accelerated IG Metall's membership losses, which instigated a broad internal debate. In

order to stabilise the membership base the issue of membership became the focus at all organisational levels and in relation to all standard tasks, projects and activities. Resource utilisation was restructured in support of these measures.² Development work on recruiting new members (or groups of members) now ranges from the systematisation of first contacts with workplaces and employees through the expansion of the existing workplace presence to member-oriented conflicts for the purpose of collective bargaining coverage.

Another key element of membership-related activities was the extension of opportunities for participation by employees and members, for example, through new forms of approach or regular, issue-related member or works council surveys. In this context a specific variant of trade union organising plays a key role. Organising is conceived here as a participation-, member- and conflict-oriented approach to the implementation of so-called 'development projects' and thus to strengthening organisational power. These efforts are supplemented by concerted efforts to reduce membership turnover. Thus local organisational units ('administrative agencies') endeavour to win back former members. Successful approaches are combined and disseminated within the framework of an internal benchmarking procedure, by which the recruitment and retention practices of particularly successful administrative agencies are used as guidelines for all administrative agencies. This takes place within the framework of an annual 'business plan process' by which the available financial and staff resources are coordinated with the target figures for membership development and the focus of local trade union policy determined for the coming year. By this and other means it has been possible to halt membership losses and successively to increase membership numbers since 2011.

4.2 Development work in the problem area of precarious employment

A second element of the revitalisation efforts was directed towards organisational development with regard to precarious employment. In the crisis that began in 2008 the limits of trade union efforts to protect employment became evident in relation to temporary employment. Since

2. For example, substantial funding was diverted via an internal 'strategic investment fund' from the executive and other departments to workplace and local recruitment.

deregulation accelerated in the early 2000s temporary work has also expanded in the branches covered by IG Metall. Despite the same performance level temporary workers are paid much less than permanent employees, besides having fewer rights and insecurity of employment. In the current crisis from 2008 almost one-third of temporary employees were laid off in IG Metall's domain. Not least in response to this development IG Metall launched a campaign under the motto 'Equal work, equal pay', in an attempt to make the public more aware of the situation of temporary workers. The campaign was part of a vision of a social restructuring of the labour market, aimed at putting precarious employment into reverse. In this way IG Metall was not only able to step up pressure on political decision-makers, but also to raise its labour market and social policy profile and credibility among both core and peripheral employees. Overall, its campaigning and collective bargaining activities were reflected in significant membership growth, with a particular rise in the organisation of temporary workers from just under 13,000 in 2010 to over 44,000 in 2012.

4.3 Measures against work intensification

A third strategic element is a labour and social policy initiative. During the financial and economic crisis not only were standard employment conditions eroded, but in many companies productivity was increased dramatically by means of work intensification. As a result, there was a significant increase in psychological ill health among the employees. IG Metall responded with a campaign against permanent work intensification (euphemistically known as 'doing more with less'). Central to this was a demand for the closure of 'legal loopholes' by means of a nationwide 'anti-stress decree' to protect against psycho-social hazards. These activities were supplemented by a campaign 'Decent jobs, decent pensions', whose aim was to disseminate among companies and obtain media exposure for the idea of 'optional transitions' to retirement, in which a number of flexible options would be set alongside the uniform retirement age of 67. While pension-law alternatives were raised in the political arena, companies were presented with a demand to adapt the workplace for the sake of ageing employees.

The activities which we have presented here selectively and only in outline raised IG Metall's profile in terms of interest representation in the workplace and as a social policy actor, both among companies and in

society as a whole.³ Success was achieved in terms of membership development and presence in the workplace. And even though it remains to be seen how sustainable these successes will be in the inevitable downturns in production and employment in the metal and electrical industry, IG Metall has made real progress in the struggle to come off the defensive. In other words, upgrading the recruitment issue, representing the interests of precarious employees and initiatives against work intensification have contributed to produce an operational professionalisation and a stabilisation of trade union organisational and negotiating power. These initiatives were based on significant strategic reorientations. In this context IG Metall's strategic and policy mix can definitely be considered evidence of successful organisational learning. In the context of the traditional routines of an industrial trade union, familiar with its membership bastions in industrial workforces, the systematic development work in relation to precarious employment can be considered a particular strategic innovation. This suggests that the trade unions, even when largely on the defensive, have a range of options open to them, offering them a 'strategic choice' by means of which they can make real progress instead of remaining stuck in a rut.

5. Gaps in trade union strategy in the European regime of authoritarian stability

This outline of the tripartite response to the German crisis can (and will) be only a first approach to corporatist developments. The empirical and theoretical diffusion of the social pacts that emerged, not only in Germany, in response to the crisis is ongoing, but far from concluded. Even the current evaluation represents rather a snapshot than verified findings. The same applies to indicators of successful trade union revitalisation efforts, outlined here on the example of IG Metall.⁴ However, it is also important to understand that the observations and conclusions presented here are provisional. In other words, we have not answered the question of whether these successes mark the end of trade unions' being on the

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3. Also important were measures directed towards differentiating in collective agreements between working time (within the framework of the so-called 'Pforzheim agreement'), workplace resistance to labour cost reductions and relocations (within the framework of the campaign 'Better instead of cheaper'), as well as activities against deterioration of working conditions in the area of skilled white-collar work.
 4. For a new analysis of IG Metall's organizing activities see Wetzel (2013); on the activities of service sector trade union ver.di see Kocsis, Sterkel and Wiedemuth (2013).

defensive and thus represent a turning point that opens up the prospect of a comprehensive societal, political and economic offensive.

In any case, it would be risky to conclude from the stabilising effects of operational professionalisation that revitalisation will necessarily be sustainable. Complex strategic problems still await a solution and the challenges facing the trade unions' strategic capabilities are enormous. These problems undoubtedly include the development of new leading economic sectors and employment groups, as well as increasing the level of trade union organisation in all branches. If success remains elusive here then lasting stabilisation of trade union organisational and negotiating power will not be achieved. But as if that was not enough, if one considers trade unions' future prospects in a European perspective questions of political strategy emerge that have not obtained promising answers in trade union strategic debate thus far. Considering the debate in Germany, one might mention the low status accorded to the equally crisis-plagued developments at the European level. Although in research on integration European unification is analysed mainly as a multi-level process, in which developments at the regional, national and European levels are regarded as interdependent elements of an overall process (see, for example, Jachtenfuchs and Kohler-Koch 2003) this multi-level perspective has as yet barely penetrated research on German corporatism. This European gap is problematic because fundamental decisions are taken at the European level that may have crucial policy implications in the member states.

5.1 New European governance and trade unions

At the end of 2010 the budget deficits and public debts of almost every country in the euro zone violated the stability guidelines of the European economic and monetary system (ECB 2011). In an opaque negotiating process distorted by national interests new economic and financial policy rules were gradually put together. It comprises agreements already reached on European governance and enhanced economic policy coordination, which by way of follow-up to the revised Lisbon Strategy were combined into the 'Europe 2020' package. The architecture of the new order is based on two institutional pillars: the first pillar consists of rules on enhanced economic policy governance and budgetary policy supervision in the euro area. This envisages, in particular, measures to boost the competitiveness of economically weaker member states and

the sanctioning of those running budget deficits. The second pillar represents a permanent crisis management mechanism, the European Stability Mechanism (ESM). It is to be activated when a country's overindebtedness threatens the financial stability of the euro zone overall and imposes strict conditions on the granting of financial aid in the form of loans (Urban 2011 and Urban 2013b: 121–158; as well as Leschke *et al.* in this volume).

This new institutional regime is working its way into areas of policy and regulation previously reserved to the member states and the social partners. This proceeds, on one hand, by narrowing fiscal options at national level. This illustrates the tendency towards technocratic solutions, which were already inherent in the Stability and Growth Pact within the framework of economic and monetary union (EMU) (avoidance of excessive deficits of more than 3 per cent or a level of public debt higher than 60 per cent of GDP). In the new regime this latent authoritarianism has attained a new quality. As a whole, the new institutional arrangement can be conceived of as a regime of authoritarian stability, which may prove to be economically counterproductive, socially polarising and politically a threat to legitimacy. What is intended to be a programme to stabilise the EU and its monetary affairs may, in the event, serve only to exacerbate its economic and societal problems and result in a precarious stability (Urban 2011). By complying with the conditions imposed with the loans the familiar sequence of problems attendant on procyclical finance policy is set in motion, leading to falling demand and growth. Declining growth, in turn, makes it difficult to obtain funds to refinance debts. This adversely affects the debtor's creditworthiness, which will immediately trigger a poorer rating by the leading agencies. This drives up risk premiums and interest on capital market bonds and thus the cost of new borrowing.

The new *authoritarian regime of precarious stabilisation* goes hand in hand with manifold violations of the interests of wage earners and a dramatic deterioration in trade union options. The guidelines for the development of wages, productivity and welfare states make serious inroads into the mechanisms of national relations between capital, labour and the state, subordinating national economic policies and the labour and social constitutions of the member states, across the board, to an excessive emphasis on competition and stability policy (see Schulten and Müller in this volume). This should set alarm bells ringing for the trade unions. In order to reduce budget deficits and public debt states intend

to drastically curtail social protection systems and cut benefits and services. Reduced compensation for life's contingencies, especially unemployment and incapacity to work, further increases pressure on wage earners and intensifies the 'reserve army mechanism' operating in the labour market. This undermines the trade unions' negotiating power. At the same time, the fiscal restrictions will lead to states ceasing to function as a *Wirtschaftsstaat* in the positive sense of pursuing economic stimulus, employment and industrial policies for the purpose of stabilising growth and employment, not to mention the inability to implement state tasks within the framework of eco-social structural change. The possibility of lending impetus to growth and employment is being given away. Wage negotiations, conducted hitherto in a spirit of social partnership, will not go unscathed, either. The verbal acknowledgement of protecting the autonomy of the social partners in collective bargaining may soon turn out to be smoke and mirrors in the face of the disciplinary and downsizing logic that is now gaining momentum. The massive contraction of national autonomous collective bargaining systems may be the inevitable consequence.

5.2 The gap in European policy strategy

The trade unions in the EU member states seem ill prepared to meet these risks. Hitherto, their policies have been directed primarily at defending their core membership against infringements of its interests and have tended to remain within the arenas of national economic and social policy. Attempts to exert influence over government policies on Europe and thus over crisis policy at the European level have been as tenuous as efforts to coordinate distribution conflicts across borders or even to network. If the trade unions wish to contribute effectively to a long-overdue change of course in Europe qualitatively new demands become evident with regard to their political mandate, but especially their European policy mandate. They are called on to play a dual role: first, as collective bargaining actors, who do their best to take advantage of the available options via an active distribution policy and second, as a political pressure group mobilising against the fatal 'austeritarian' mania of the Troika and for a redistributive economic policy that creates real value.

To date, there has been no escaping the striking discrepancy between what is needed and what the trade unions have actually been doing. To be sure, this is due to their lack of clout in Europe. At the same time,

however, it indicates conceptual failures emerging from a painful gap in European policy strategy. Their impact in the euro zone and on competitive structures between the euro countries is not adequately reflected in either questions about the future in collective bargaining or in the formulation of national collective bargaining demands, nor are the European trade unions' collective bargaining goals coordinated, not to mention strategic ideas about transnational mobilisation against austerity policy. Finally, there is little systematic consideration of how the national and the European levels could be connected by policy measures that take into account the specific conditions facing the trade unions in their national contexts and which influence their ability to assert themselves more strongly at the European level. If the different conditions in the various 'trade union worlds' (on this see Lehndorff on trade unions in this volume) are not recognised and the strategic gaps in European policy are not closed it will not be possible to amass sufficient political clout against capital and European decision-making elites. Hitherto, the demands referred to here have not even been adequately formulated, never mind worked on with the necessary assiduity. This failure must urgently be put right.

6. Outlook: open strategic and research questions

To sum up, despite signs of a trade union revival the crisis so far can hardly be described as a positive 'turning point for labour' (Baccaro 2010). The trade unions have not benefited from neoliberalism's political and ideological fall from grace. Evidently, not only the defensive stance in which the left had got stuck in general but the erosion of trade union power in particular made it difficult for the organisations representing dependent labour to make a rapid come-back (Boyer 2010; Crouch 2010). However, there are indications that some trade unions have experienced something of a revival since the crisis. We cited IG Metall as an example. Clearly, organisational learning may take place under crisis conditions and successful organisational revitalisation may occur by means of innovative practical strategies. An interim summary may thus appear contradictory: on one hand, the trade unions have by no means ceased to be on the defensive, but on the other hand, this defensive position is neither total nor inescapable.

What conclusions can be drawn from this ambiguous verdict on the trade union strategy debate? The outlined problems show that correcting the

asymmetrical distribution of income and power before and during the crisis, as well as the Europeanisation of trade union interests should be given high priority on the trade union agenda. On top of that efforts must be made to revitalise trade union power, because success is feasible with regard to distribution and European policy only on condition that sufficient negotiating and organisational power can be deployed. In light of such demands it appears questionable whether the social pacts of crisis corporatism represent an appropriate framework for coping. A positive re-regulation of the labour market and an egalitarian redistribution of income and wealth may rapidly prove to be incompatible with corporatism because they conflict too sharply with the interests and power claims of the other actors. At the same time, we cannot dismiss the danger that the logic of national social pacts may be a stumbling block for the long overdue transnationalisation of trade unionism. If, after the worst of the crisis is over, the crisis corporatist alliances continue in the form of a resumption of location pacts within the framework of competitiveness-oriented corporatism the very trade union resources required for the strategic Europeanisation of trade union policy will be tied up elsewhere.

It is difficult to discern where the limits of corporatist interests really lie. Research into the achievements and long-term effects of crisis corporatism is still in its infancy. It is conceivable that crisis corporatism is rather a short-lived and temporary phenomenon that emerged at the height of the crisis as a result of corporatist remnants in the German labour relations model and specific features of the shock experienced by financial capitalism, only to evaporate in the course of the recovery of economic growth. Thus crisis corporatism would turn out to be a variant of corporatism that ceases to exist with the end of the crisis, thus differing from its corporatist predecessors also in terms of its duration. However, whether the crisis of financial market capitalism is really at an end, whether the revitalisation of trade union power lasts and how the strategic preferences of corporatist actors in Germany and Europe as a whole develop are far from certain. There appears to be no shortage of potential research questions.

Only one thing is certain, namely that any successes that trade unions might register in capitalist societies will not depend solely on their strategic will, but also on the realities of the balance of power. It thus matters a great deal what power resources trade unions have at their disposal. This applies both within and outside any tripartite arrangements, as well as with regard to conflict-oriented and militant strategies, on one hand,

and compromise and dialogue-oriented strategies, on the other. Thus the regeneration of trade union power in financial market capitalism will become a general condition of a successful assertion of interests, regardless of whether 'boxing or dancing' is the appropriate metaphor (Huzard, Gregory and Scott 2004).

Strategic efforts to this end must be developed and implemented in tandem with national variants of the European employment model and thus in accordance with the relevant production, employment and welfare systems (Bosch, Rubery and Lehnendorff 2007a). Under the circumstances of the German model the following aims have been designated as particularly important:

- (i) expansion of trade union embeddedness in the workplace and the de-precarisation of work;
- (ii) increasing the general level of trade union organisation and the organisation of new groups of wage earners;
- (iii) institutional reform of sectoral collective agreements and of labour and social regulation;
- (iv) expansion of trade union influence in the national economic and social policy arenas; and finally,
- (v) strengthening of communications with regard to trade union crisis policy and its normative models (Urban 2005 and 2010b).

However, regardless of the institutional specificities of the national regime the trade unions' conception of their strategic role could determine whether the strategic challenges are recognised as such and properly tackled. This is unlikely to succeed in the form of a structurally conservative blockade to salvage whatever can be defended both during and subsequent to the crisis. Furthermore, even persevering in the role of cheerleader for modernisation and facilitator during the crisis is likely to come up short with regard to the relevant challenges. More promising appears to be a conception of the trade union role as a *constructive veto player* (Urban 2005). This conception assumes that not only the transition from the Fordist model to a new socio-economic development model, but also the exit from the crisis of this model will take place via distribution and negotiation conflicts based on power; furthermore, the ability to adequately mobilise power resources will determine one's ability to assert oneself as a key player in arenas of conflict. The same applies to firefighting conflicts with regard to inadequate strategies for dealing with problems and (partial) successes in that regard within the frame-

work of a strategy for gradually overcoming the trade unions' defensive stance. Nevertheless, the veto power based upon this will be deployed 'constructively' in the sense that it is used not to conserve status-quo structures but to contribute towards the reconstruction of the socio-economic development model. Side by side with the mobilisation of veto power to block strategies purportedly aiming to overcome the crisis but in fact likely to exacerbate it, is the mobilisation of power for change in the implementation of policy ideas aimed at solving problems.

It is also desirable to consider the far from trivial implications of the corporatist involvement of the trade unions for internal decision-making. Crisis corporatism is also characterised by a tension between an orientation towards influencing policy and a conflicting membership-oriented logic (Streeck 1999: 223–245). Thus being too closely and for too long involved in social pacts that blatantly distribute the costs and benefits of the crisis unequally may jeopardise the internal democracy of the trade unions. In other words, the deeper the implication of the trade unions in corporatist arrangements and the higher the price to be paid for asserting trade union interests, the stronger the inclination of federation leaderships might become to try to influence internal discussions and decision-making processes in order to minimise conflicts between emerging internal opinion and the requirements of corporatist alliances and to maximise trade unions' ability to comply with their commitments. Measures of this kind to shape internal processes could rapidly impose constraints on the proper articulation of members' interests and thus damage internal democracy (for a stimulating contribution on this see Molina 2008). Whether these risks to democracy can be countered by means of more decentralised decision-making structures and more membership participation, or whether these measures will instead result in the obstruction of the tripartite model needs to be examined by policy research with a clear eye for practical implementation.

All in all, the scholarly and the trade union policy evaluation of crisis corporatism reveal a broad field for social science research and trade union strategic debate. This involves continuing scholarly work on corporatism and developing a terminology that expresses the specific features of the macroeconomic context, the interests involved and the actors' power endowments. For that purpose we have put the concept of crisis corporatism up for discussion. These efforts are intended to link up with the current debate on the new capabilities of nation states. If the scepticism concerning the thesis of the return of more capable states in the crisis

is substantiated (see Hassel and Lück 2010) this is unlikely to leave the reliability of state promises and the chances of success of crisis corporatist alliances unaffected. Finally, the revitalisation of trade union power represents a project that requires above all internal efforts. However, there is much to suggest that they should be seen in a more comprehensive, Europe-wide context, paying due attention to alliance formation. The strategic gain for the trade unions could be that they are able to supplement their unsatisfactory power resources with alliances with other powerful movements (Hyman and Gumbrell-McCormick 2010b: 328). Neglect of these tasks would come at the cost of keeping the trade unions on the defensive.

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Towards 'Europe 2020'? Austerity and new economic governance in the EU

Janine Leschke, Sotiria Theodoropoulou and Andrew Watt

1. Introduction

The financial crisis that broke out in 2008 has turned into an economic and public debt crisis that has swept the EU, with a severe impact on the economies and labour markets of member states. Output growth turned negative in several countries and stagnated elsewhere; unemployment rose; and public debt and deficits soared. Partly in response to the crisis and partly within the framework of a longer-term growth and reform agenda, the EU spelled out the Europe 2020 Strategy in 2010, which for the first time put inclusive growth on an equal footing with smart and sustainable growth – at least on paper. To that end, a headline target of moving 20 million people out of poverty by 2020 was set. The strategy calls for structural reforms in several areas, as well as for steering the public finances of member states onto a sustainable path as soon as possible.

Moreover, in response to the debt crisis that has been threatening the very existence of the euro zone and as a complement to the Europe 2020 Strategy, the architecture of the EU's economic governance has come under scrutiny with the aim of introducing reforms that would strengthen it against similar crises in the future. At the same time, the euro-zone member states have been trying to contain the public debt crisis which, at the time of writing (September 2013), has spread to seven member states and has become a systemic threat to banking systems in the EU.

National policies in the context of the Europe 2020 Strategy and the new economic governance are to be streamlined and coordinated within what is now called the 'European Semester', which is essentially the annual policymaking cycle in the EU. However, both the economic governance reforms and the austerity measures pursued as a response to the debt

crisis have attracted criticism for pushing the European economy into a double-dip recession and strangling growth for several years to come. This risks undermining the objectives of the Europe 2020 Strategy, including that of inclusive growth.

This chapter analyses whether the recent EU economic governance reforms and the austerity measures are likely to affect the prospects of achieving the headline target of lifting 20 million people out of poverty. Fiscal austerity, as pursued in several member states, has been delaying output and employment recovery, leading to prolonged and structural unemployment which is associated with detachment from the labour market. According to the Europe 2020 Strategy, the means of achieving inclusive growth are increasing employment, improving skills and fighting poverty. In this chapter, we focus on poverty because employment creation and improved skills have failed to deliver in terms of reducing poverty in the context of the Lisbon Strategy (Cantillon 2011). Moreover, in the face of the ongoing creation of substandard employment, with its danger of keeping people in low-wage employment, the development of poverty figures tell us more about inclusion than the mere monitoring of employment rates or developments in skills.

The chapter is structured as follows. In Section 2, we provide an empirical picture of the impact of the crisis on labour market outcomes and public finances in order to get a sense of the problems and put into context the macroeconomic policy directions that the new economic governance and initiatives to resolve the crisis propose. In Section 3, we present the policy responses to the crisis and critically evaluate their potential to deliver growth. In Section 4, we analyse the Commission recommendations to member states in the context of the European Semester, the medium-term policy plans of member states in terms of – in particular – social spending and the measures already taken as part of the fiscal austerity packages in several member states in order to assess whether fiscal measures undermine and/or override measures for reducing poverty. Section 5 concludes. To support our arguments, we draw on comparative data sources, such as the European Labour Force Survey and national accounts, official EU level and national policy documents and evidence from national experts on austerity programmes (Matsaganis and Leventi 2011; Theodoropoulou and Watt 2011).

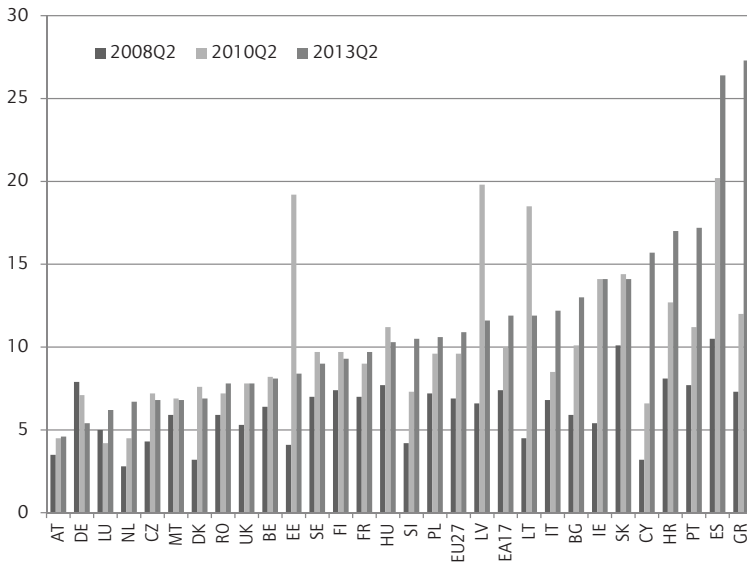
2. The economic crisis in Europe

In this section, we provide an empirical view of the impact of the crisis in Europe with regard to output, employment and unemployment. We also review the evolution of European governments' public debt and budget balances. All these are crucial parameters for assessing the economic governance reforms and the fiscal austerity measures in terms of their potential to help tackle the current economic crisis and support the Europe 2020 Strategy in meeting its poverty headline target.

2.1 Bleak labour market developments

EU27 average unemployment stood at 10.9 per cent in the second quarter of 2013, 4 percentage points up from the second quarter of 2008 (Figure 1). Employment fell in the same period by 1.7 percentage points

Figure 1 Development of unemployment rates, 2008Q2, 2010Q2, 2013Q2



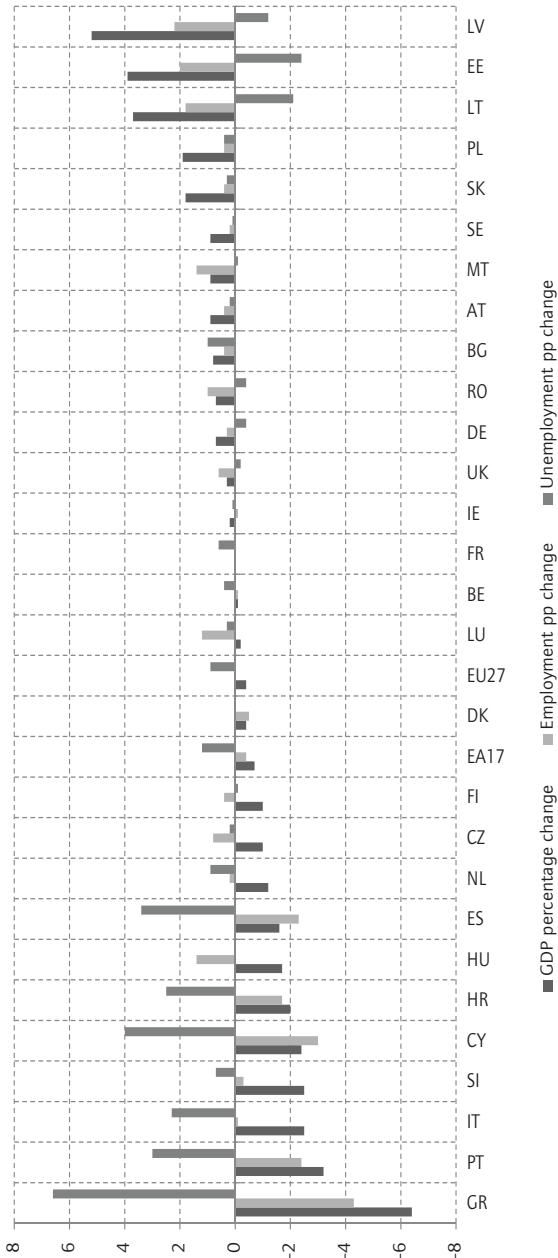
Note: Unemployment rates for population aged 15–64 years. Figures for the second quarter used as 2013 annual figures not yet available.

Source: Eurostat online data base (Labour Force Survey).

on average. The labour market impact of the large output shocks – average output in the EU fell by 4.3 per cent in 2009 – was thus considerable. At the same time, as Figure 1 illustrates, there has been significant variation in developments in unemployment (and employment) rates in Europe. Particularly Spain and Greece, Ireland, Portugal, Cyprus and the Baltic countries saw huge increases in unemployment and large drops in employment and – with the exception of the Baltic countries, which have recently seen considerable improvements – were among the countries with the highest unemployment rates in 2012. Looking at the initial crisis period (second quarter of 2008–second quarter of 2009) in the Baltic countries rising unemployment was coupled with considerably larger than average falls in output, whereas unemployment in Spain, for example, increased markedly despite below average falls in output (for details, refer to ETUI/ETUC 2012). This points to the absence of such things as working time measures, active labour market policies or early retirement and other exit schemes that can act as buffers. The working of such buffers was particularly evident in the case of Germany, one of the few countries that saw unemployment dropping despite an above average drop in output (for details on the operation of buffers in the crisis, see Leschke and Watt 2010).

Looking at the most recent crisis phase, output fell on average by 0.4 per cent (2012), whereas the previous two years had seen average growth. Also, unemployment was still rising in most countries and employment declining in 10 countries. Figure 2 presents the most recent developments in terms of output, employment and unemployment (2012 compared with 2011). Output is still or again declining in 14 countries, notably in Greece and Portugal, whereas some countries are showing output growth of more than 3 per cent, notably Latvia, Estonia and Lithuania, albeit following remarkably large output losses. In this one year period, Greece, Cyprus, Spain and Portugal saw unemployment increase by more than 3 percentage points and by as much as 6.6 percentage points in Greece. At the same time, employment was declining still further, especially in Greece, Cyprus, Portugal and Spain. Looking at the five countries that initially experienced the biggest labour market impact from the crisis we see in particular Spain and, to a lesser degree, Ireland still doing comparatively badly. This contrasts sharply with the Baltic countries where we see major output growth in the most recent period (following the massive contraction there) and strong increases in employment and decreases in unemployment. It is worth noting that the Baltic States at the same time experienced large outflows of labour (Galgóczi *et al.* 2012).

Figure 2 GDP,* employment and unemployment rates, 2012 (change compared with 2011)



Notes: * GDP as used in Figure 2 refers to gross domestic product at market prices. Employment and unemployment rates for population 15–64 years of age.
Source: Eurostat online data base (national accounts and Labour Force Survey).

All in all, the picture that emerges from output and labour market developments in the EU from the beginning of the economic crisis until today is bleak. The end of the initial downturn did not do much to reverse the initial employment losses. We are now in the middle of a double-dip recession, with evidence of deep-seated problems in the financial sector, against the background of the unresolved sovereign debt crisis (although the picture may be brighter in individual countries).

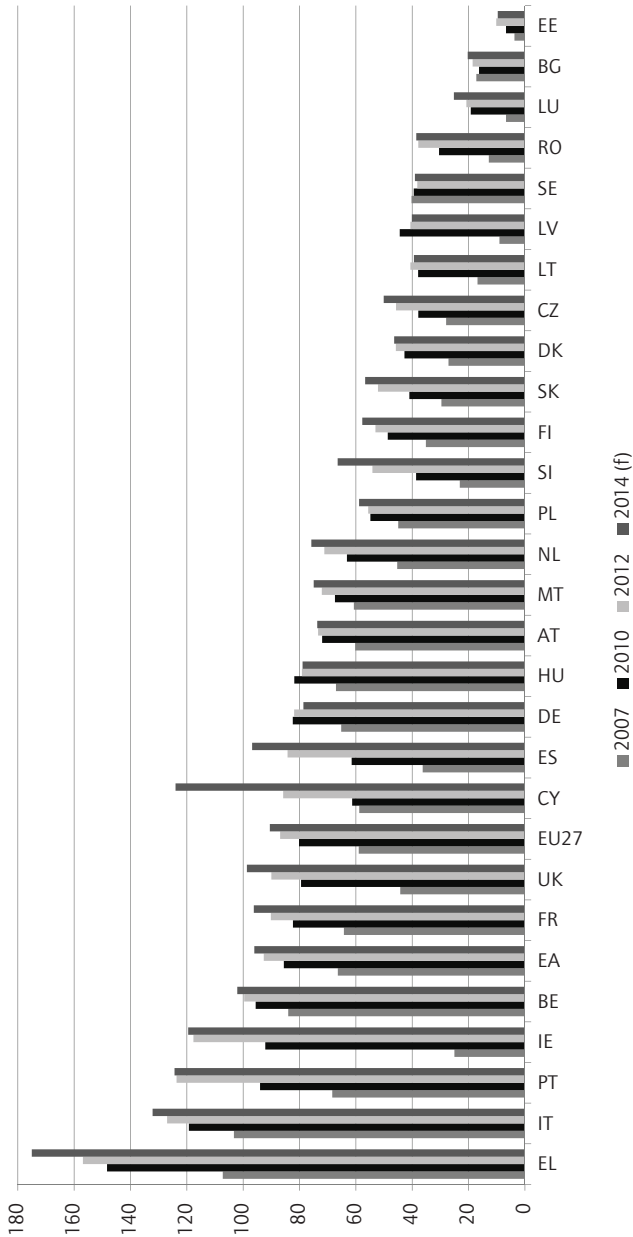
There are negative feedback loops between the state of the labour market, the vulnerability of financial institutions and the sovereign debt crisis. In the short term, uncertainty over growth and employment restrains bank lending and firms' recruitment. This also makes it more difficult to consolidate public finances, which creates further uncertainty. On the labour market the concern is that lower employment and higher unemployment rates will become entrenched, as happened for instance in the mid-1990s.¹ If the appropriate macroeconomic demand-side measures are not – or cannot – be deployed, the use of market-oriented structural policies increases the risk of poverty and social exclusion. We return to this issue in more detail below.

2.2 The crisis and the state of public finances

The economic crisis that began in the last quarter of 2008 has had substantial and varied effects on public finances in European countries (Figures 3 and 4). On average, the gross public debt to GDP ratio in the EU27 rose from 59 per cent in 2007 (66 per cent in the euro area) to 87 per cent in 2012 (93 per cent in the euro area), while it is expected to rise further to 91 per cent by 2014 (96 per cent in the euro area).² Several EU member states saw their public debt to GDP ratios rise to levels that wiped out the fiscal consolidation of the past 25 years or more. Most notably, Ireland's debt to GDP ratio rose by 93 percentage points from 25 to 118 per cent between 2007 and 2012 and it is expected to reach 119 per cent of Irish GDP in 2014. Portugal, Spain and the United Kingdom saw rises in their gross debt to GDP ratios of 46–55 percentage points. The Greek ratio climbed from 107 to 157 per cent between 2007 and 2012, but only following the 'voluntary' haircut that was agreed in October 2011, and it is expected to go up further to 175 per cent of GDP by 2014.

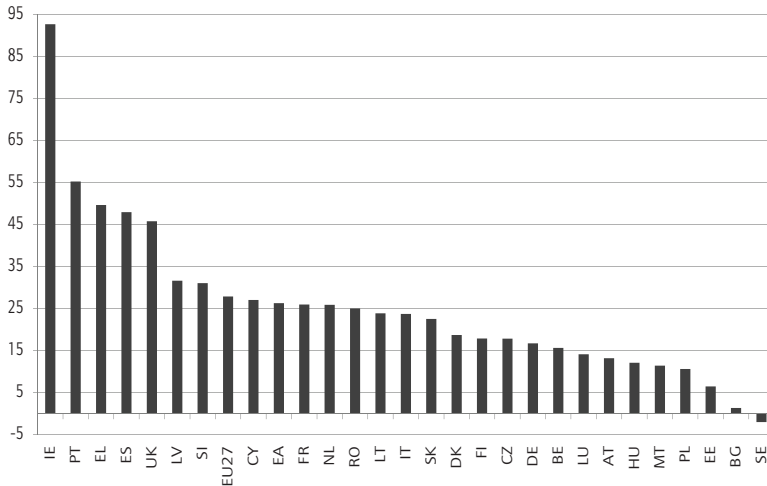
1. www.social-europe.eu/2011/08/rising-unemployment-please-not-199596-all-over-again/
2. All figures and forecasts from the AMECO database.

Figure 3 Gross public debt to GDP ratio, EU, 2007, 2010, 2012, 2014



Source: AMECO data.

Figure 4 Change in debt/GDP ratio, 2007-2012 (percentage points)



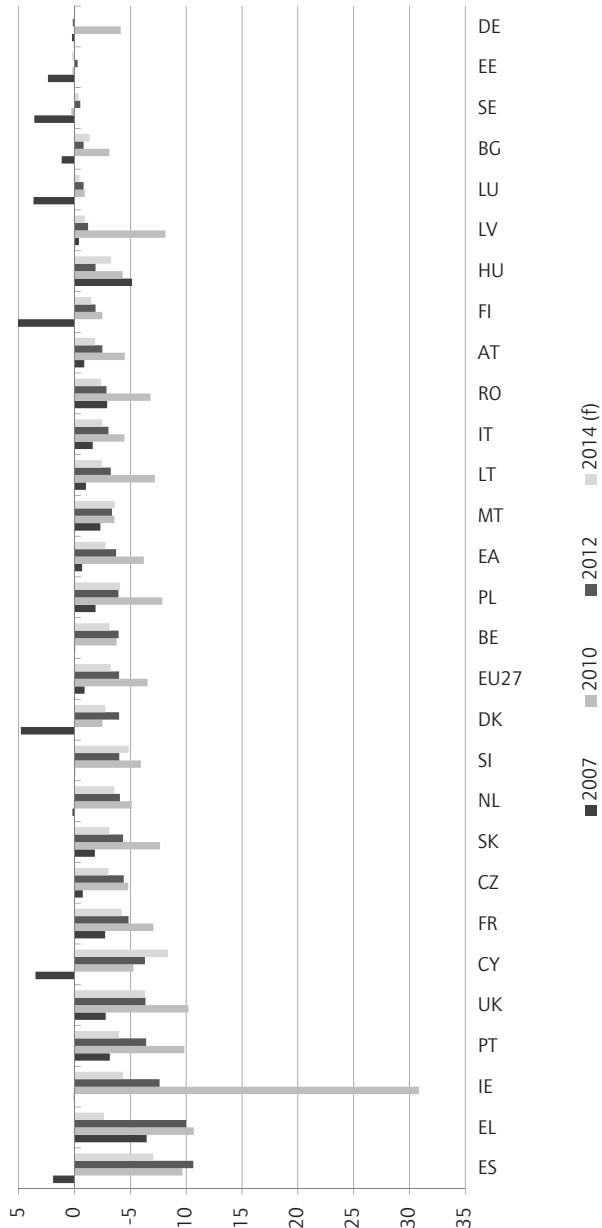
Source: AMECO data.

In the United Kingdom, the ratio increased from 44 to 87 per cent during the same period and is forecast to reach 91 per cent by 2014. Portugal and Spain also suffered debt to GDP increases of 48 to 55 percentage points between 2007 and 2012, although only the Portuguese ratio has exceeded 100 per cent of GDP, with that of Spain remaining below the EU/euro area averages.

The increases in the gross debt to GDP ratio reflect two factors: first, the deterioration of government budget balances across Europe due to the crisis, reflecting the operation of the automatic stabilisers (Watt 2011), the discretionary stimulus packages (Watt 2009) and the measures to bail out the financial sector; secondly, the contraction of GDP. The average budget deficit rose from 0.9 per cent of GDP in 2007 (0.7 per cent in the euro area) to 4.0 per cent in 2012 (3.7 per cent in the euro area) (Figure 5). Although these average figures conceal a wide variation, only a minority of 11 member states complied with the Stability and Growth Pact's 3 per cent deficit limit in 2012.

As the credit crunch/financial crisis of 2007–2008 turned into a real-economy crisis, and doubts about the capacity of Greece to repay its debt

Figure 5 General government budget deficit, EU, 2007, 2010, 2012, 2014 (% of GDP)



Source: AMECO data.

arose in the markets, the failure of European leaders to give a credible and timely guarantee that a member of the euro zone would not (partly) default and the refusal of the ECB to undertake the role of lender of last resort for governments sparked contagion and a debt crisis (DeGrauwe 2011a). It is true that the Greek debt to GDP ratio was relatively high in 2009; however, its sustainability depended not only on this ratio but also on future government balances, the growth rate of the economy and the interest payments the government has to incur in order to keep rolling over its debt. The lack of guarantee meant that the interest rate required from the Greek government to keep on rolling over its debt started to increase, turning what could have been a liquidity problem into a solvency problem (DeGrauwe 2011b). This lack of confidence then spread to other euro-zone members with either high debt to GDP ratios or rapidly increasing government budget deficits. By early 2011, Ireland and Portugal had also sought financial support from the EU and the IMF in order to keep rolling over their public debt, while in the summer of 2011 Spain and Italy also faced very high yield spreads for their government bonds compared with German ones. Eventually, in the summer of 2012 Spain sought financial support to recapitalise its banks, while in 2013 Cyprus became the fourth member state to receive a government bail-out conditional upon a severe adjustment programme.

Due to the failure to provide adequate solutions the Greek, Irish and Portuguese debts continued to rise (in the Greek case, even after the 'haircut'), because under the financial 'support' programmes their governments have been effectively loaded with more debt, carrying relatively high interest rates (which were lowered following the European Council meeting of July 2011). At the same time, the severe austerity programmes that were imposed as a condition for receiving aid plunged the three economies into major recession, which worked counter to fiscal consolidation by reducing public revenues, raising benefit expenditure and making spending cuts all the more difficult politically. Recession in those countries, but also in member states facing difficulties financing their public debt in financial markets, has taken a toll on banking systems. The number of non-performing loans increased, deteriorating the balance sheets of the banks that had granted them and thus putting into question their soundness. This created a vicious circle between a banking and a fiscal crisis. Expectations on governments to step in and bail out ailing banks increased negative sentiments on the sustainability of public finances, while governments' financial difficulties fuelled further fears about the soundness of banking systems.

Summing up, we can see profound effects on European labour markets and government budgets from the crisis with, at the same time, great variation between countries. Against this background we now turn to consider the policies implemented in Europe to the extent that they are driven by European policymaking initiatives and processes. First, we describe the main policy initiatives taken at European level since the crisis, before analysing how they have affected – and will continue to affect – national policy choices and also policy outcomes.

3. Policy responses to the quest for growth and the economic crisis: the Europe 2020 Strategy and economic governance reforms

3.1 Europe 2020 Strategy

Partly in response to the crisis, but partly within the framework of a longer-term reform agenda, the European Union has embarked on a complex, multi-layered process of changing the framework within which not only economic but also a wide range of employment-related, social and other policies are designed and implemented by both member states and the European institutions. This process is ongoing. In this section we summarise some of the key developments, focusing on those particularly relevant to the issue of inclusive growth and the headline target with regard to poverty.

The Europe 2020 Strategy is the successor to the Lisbon Strategy, launched in 2000, which ended formally in 2010. Lisbon formulated the strategic goal of becoming ‘the most competitive and dynamic knowledge-based economy in the world, capable of sustainable growth with more and better jobs and greater social cohesion’; this goal was underpinned by a number of EU-level targets. The Europe 2020 priorities and strategy closely resemble those of Lisbon despite the fact that the European Union was not able to deliver on the targets (European Commission 2010a) and probably would not have done so even in the absence of the economic crisis (for a critical account, see Pochet 2010).

The Europe 2020 Strategy puts forward three ‘mutually reinforcing’ growth paradigms: smart growth through knowledge and innovation; sustainable growth entailing resource efficiency and a greener and more competitive economy; and inclusive growth, focusing on high em-

ployment and social and territorial cohesion (European Commission 2010d). Thus, even the social and environmental issues are framed in terms of the growth paradigm. Five headline targets for 2020, covering employment, R&D, climate/energy, education and poverty for the EU as a whole, reflect this strategy.³ The Council's 10 integrated guidelines for implementation of the Strategy (six focussing on economic policies, three on employment and one on social inclusion and poverty reduction) are supposed to steer and guide reforms in the member states, whereby they are subject to conformity with the fiscal rules of the Stability and Growth Pact (European Commission 2010b). The so-called seven flagship initiatives spell out the policy measures to be undertaken jointly by EU-level and national actors, which concern the policy areas regarded as most important.

In response to the economic crisis that has revealed the interdependencies and spillovers between different areas, the Europe 2020 Strategy seeks to align macroeconomic policy developments and structural reforms within the framework of the so-called 'European semester'. Stability and Convergence Programmes (which focus on fiscal issues) and National Reform Programmes (covering a wide range of structural policies) are now to be prepared at the same time in the first half of each year to ensure more coherence in reporting, evaluation and recommendations on thematic, as well as on economic and budgetary issues. These can then be fed into the finalisation of national budgets (ex ante policy coordination).⁴ The aim is to strengthen budgetary discipline and promote macroeconomic stability and growth in line with the Europe 2020 aims.

In the social and employment field, most European coordination takes place through soft law mechanisms, namely the open method of coordination, (OMC), with little leverage for putting pressure on member states to implement or desist from certain policies. As part of the OMC, recommendations are issued (see below) but there are no sanction mechanisms.

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3. The targets are as follows: an employment rate of 75 per cent for people aged 20–64; 3 per cent of EU GDP invested in R&D; a list of climate/energy targets; reducing the proportion of early school leavers to below 10 per cent and at the same time increasing the share of young people with tertiary education to at least 40 per cent; and reducing the number of people at risk of poverty in the EU by at least 20 million.
 4. This is a further step towards aligning various policy fields. The process started after the mid-term evaluation of the Lisbon Strategy in 2004 when economic, employment and social policies were better integrated by implementing common guidelines and using a common reporting system, the National Reform Programmes.

The components of inclusive growth, in the Europe 2020 definition, are increasing employment, improving skills and fighting poverty (European Commission 2010d: 16–18). Under the general heading of poverty, the focus is on child poverty but also the working poor and the exposure of the unemployed to poverty. It can be considered a step forward that the social dimension has been integrated into the overall Europe 2020 Strategy, but the fact that it is so closely intertwined with employment issues makes it uncertain whether and how member states will address the social inclusion guideline (Zeitlin 2010: 262).

The new Europe 2020 poverty target – to lift 20 million (or one in six) people out of poverty and social exclusion – reflects the need for political compromise (for details, see Mailand 2011). This is illustrated notably by the fact that the EU27 target is measured on the basis of three combined indicators: at-risk-of-poverty rate,⁵ severe material deprivation rate⁶ and households with very low work intensity.⁷ This combination of monetary (relative income poverty) and non-monetary (material deprivation and exclusion from the labour market) components of poverty is supposed to reflect the multifaceted nature of poverty.⁸ A key point is that member states can choose whether they want to use the composite EU definition for monitoring poverty or set targets on the basis of a subset of the three indicators or on the basis of national indicators reflecting the specific country situation. Most countries have applied the EU definition but an important subset of countries use other definitions, the most popular being the 'at-risk-of-poverty rate' (for a provisional list, see Council of the European Union 2011: 3–4).

Previous assessments of the Lisbon Strategy that also focused on growth, employment creation and skills upgrading suggest disappointing outcomes with regard to poverty (Cantillon 2011). Other research has also pointed out that substantial inequalities exist within groups of people

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5. Persons with an equivalised disposable income below the at-risk-of-poverty threshold, which is defined as 60 per cent of the national median equivalised disposable income after social transfers.
 6. Severe deprivation is defined as experiencing at least four out of nine deprivation items. The deprivation items are as follows: cannot afford to; pay rent or utility bills; keep home adequately warm; face unexpected expenses; eat meat, fish or a protein equivalent every second day; take a week's holiday away from home; or buy a car, a washing machine, a colour TV or a telephone.
 7. Defined as persons aged 0–59 living in households in which adults worked less than 20 per cent of their total work potential during the past year.
 8. For detailed information on the social dimension of the Europe 2020 Strategy see Council of the European Union, 18 February 2011.

with similar skill levels (Franzini 2011). In other words, employment growth and skills acquisition have been shown to be far from unequivocal paths to more social cohesion, even when macroeconomic conditions were more conducive than currently. Depressed output growth, massive increases in unemployment and pressures to decentralise collective wage bargaining are likely to make these links even weaker.

3.2 Economic governance reforms

The Europe 2020 Strategy was drawn up and launched at a time when the European economy – and especially the euro zone – was facing the deepest economic crisis since its inception. In the case of the euro zone, the debt crisis exposed the shortcomings of the economic governance architecture put into place starting in 1992.

A succession of reforms has been implemented over recent years, with initiatives from the European institutions increasingly overlapping with intergovernmental initiatives. The result is a highly complex and confusing institutional mix.⁹ The impact of these reforms will become apparent only in the coming years. We seek here to bring out the most important developments and provide an assessment focusing on the impact on inequality and inclusive growth.

The direct European support to countries in difficulty consisted of three main elements. First IMF/EU/ECB (the so-called Troika) financial support packages were put together for Greece, Ireland and Portugal, followed in 2013 by Cyprus. Secondly, the European Financial Support Facility (EFSF) was established as a temporary vehicle supporting euro-zone governments facing prohibitively high interest rates for financing their debt in the markets. Following the creation of a permanent fund, the European Financial Stability Mechanism (ESM), in October 2012 the activities of the EFSF have been gradually wound down. The two funds issue bonds, the proceeds of which are lent on to countries at reduced interest rates in return for fiscal and structural reform commitments. Thirdly, the ECB launched the Securities Markets Programme (SMP) under which it began buying euro-zone governments' bonds.

9. An official overview is provided here: http://ec.europa.eu/economy_finance/economic_governance/

At the same time, the spreading of the crisis and its implications forced a rethink with regard to the economic governance institutions and procedures that were in place, leading to a number of important changes at European level.

During 2011 a bundle of economic governance measures, known as the 'six-pack', went through the legislative process and entered into force on 13 December. Four of the sets of measures were related to the coordination of fiscal policy and involved strengthening the provisions of the Stability and Growth Pact. The other two related to the issue of 'macroeconomic imbalances' – the competitiveness and current account imbalances that had built up prior to the crisis in the euro zone. In May 2013 the fiscal rules were supplemented further, for euro countries only, by the so-called 'two-pack', which did not tighten the substance of the regulations but did intensify the frequency of the monitoring and surveillance processes.¹⁰ As if this were not enough, in the interval all members of the EU except the United Kingdom and the Czech Republic signed the intergovernmental Treaty on Stability, Coordination and Governance in the Economic and Monetary Union. More popularly known as the Fiscal Compact, the agreement was signed in March 2012 and came into force, for the 16 countries that had at the time ratified it, on 1 January 2013. The main feature of the fiscal compact is an obligation to institute an independent fiscal council at national level and commit to running a balanced structural budget (defined as less than 0.5 per cent of GDP unless debt is significantly below 60 per cent).

Overall, the plethora of overlapping new fiscal instruments considerably reinforce the surveillance of fiscal policy under the Stability and Growth Pact (SGP). Latitude in interpreting real-time deviations from a country's MTO (medium-term objective) has been reduced. A notable change is an insistence on compliance with the debt criterion (60 per cent of GDP), which had previously essentially been ignored and can now constitute grounds, irrespective of the size of the current deficit, for launching the Excessive Deficit Procedure. Countries will be required to achieve rapid downward adjustment towards the threshold (one-twentieth of the gap between the current and target debt-to-GDP ratio per year). The sanctions regime under both the preventive and corrective arms of the Pact is to be tightened, with a more graduated range of sanctions, coupled with

10. See http://europa.eu/rapid/press-release_MEMO-13-457_en.htm/

the application of the reverse voting mechanism that makes it harder for member states to block a Commission recommendation to impose sanctions: the member state threatened by sanctions will have to obtain a qualified majority to overturn the recommendation (as opposed to a qualified majority being necessary in order to endorse the sanction recommendation). Sanctions can now be imposed in an amount up to 0.5 per cent of national GDP. Particular regard is to be paid to the expenditure side of the budget, with a norm of linking expenditure to the medium-term rate of economic growth. More attention is also to be paid to fiscal institutions in the member states in order to improve the basis for decision-making and ensuring the provision of correct data.

Surveillance of member states is also to be substantially broadened in comparison with the previous narrow emphasis on the fiscal stance. A new, so-called excessive imbalance procedure (EIP) was introduced under the six-pack, modelled on the excessive deficit procedure in the SGP. Under the EIP the competitiveness and current account positions (see Box 1) of all member states are assessed against a 'scoreboard' of relevant indicators. The Commission and the Council can make recommendations to member states if the imbalances are held to be excessive and injurious. Like the SGP there is also a corrective arm under which member states (in the euro area) can be sanctioned for failing to comply with recommendations. A country can be required to deposit up to 0.1 per cent of GDP with the European Commission which, in the case of repeated non-compliance, can be converted into a fine. Decisions on sanctions are taken by the Council, but subject to the new 'reverse majority' procedure described above.

In *procedural* terms the European semester and other efforts at strengthening the coordination of economic policymaking can be welcomed as bringing about much needed policymaking coordination. It is a step in the direction of 'economic governance' that many from the outset considered indispensable for the operation of a monetary union. The problem, notably in the first year of its operation, was the misguided *substantive* thrust given by the first Annual Growth Survey. One important focus of the reforms is a substantial intensification of the longstanding but largely unjustified and unhealthy European obsession with fiscal deficits and public debt. This not least raises the danger of a dangerous intensification of fiscal austerity and neglecting cyclical stabilisation. The focus on the expenditure side is likely to have negative distributional implications and thus is inimical to inclusive growth.

The attention to be paid to macroeconomic imbalances is, in principle, justified in light of what has been learned during the crisis (see Box 1). However, there are serious concerns about how wage setting at the national level is supposed to be 'policed' by policymakers at both EU and national level. The scoreboard used to operationalise the EIP imposes adjustment one-sidedly on deficit countries, rather than taking a symmetrical approach to the correction of imbalances. This is most obvious in the case of the monitoring of current account imbalances themselves, which are considered problematic for deficit countries in excess of (minus) 4 per cent, but for surplus countries only above 6 per cent (in each case taking three-year averages). In the case of unit labour costs there is only an upper threshold. Wages, it seems, can by definition never grow slowly enough. Above all, the reforms represent a missed opportunity to use the crisis to make changes that would enhance growth and employment opportunities in Europe and improve the welfare of European citizens. Notably absent from the reforms is any reference to the role of monetary policy within economic governance. Other matters urgently requiring reform – such as limiting tax competition between EU countries – are not addressed.

Overall, Europe has developed a bewildering array of overlapping policy responses in the area of economic governance. Beyond this confusion, none of the measures proposed, singly or jointly, come close to resolving the key problems facing the euro area.

In the context of the present discussion, which focuses on the prospects for inclusive growth, it can be concluded that the economic governance reforms are based to a considerable extent on a misdiagnosis of the problem ('it's mostly fiscal' and more market-oriented structural reforms are needed). This never constituted an adequate response to the crisis and constrained, in the short run, any prospect of economic growth and ultimately pushed the EU into a renewed downturn. Exacerbating the shift to Continent-wide austerity destroyed any prospect of a swift recovery of demand and output. It also promoted policies (expenditure-side forced consolidation, decentralisation of collective bargaining and a 'make work pay' approach to labour market policy) that will tend to make any growth that does occur less 'inclusive' (see also Section 4). Finally, it risks embedding retrogressive policies in the longer term (such as a debt brake), thereby depressing public investment.

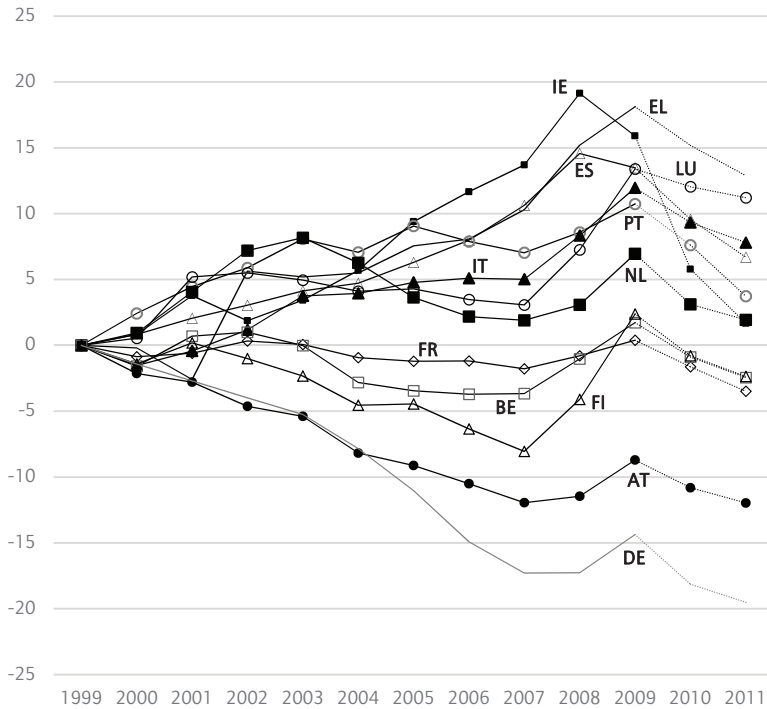
Box 1

One widely drawn lesson of the economic crisis is that **current account imbalances** are a problem, not only at the global level (for instance, the United States and China), but also between countries that share a common currency.¹¹ Such imbalances arose because of the workings of EMU (see Theodoropoulou and Watt 2011). On joining EMU, previously high-inflation European countries on the southern and western periphery that had had high interest rates benefited from a sharp fall in borrowing costs, setting off a – seemingly – virtuous circle: these fast-growing, high-inflation economies enjoyed relatively low real interest rates (the common ECB rate minus their high inflation rates). This stoked up economic activity, also by driving up asset – especially house – prices, which in turn stimulated the economy through various wealth effects. Meanwhile, slow-growing, low-inflation countries were mired in a mirror-image vicious circle, facing slow growth and low inflation with relatively high real interest rates. This dichotomy was exaggerated by the one-sided nature of the Stability and Growth Pact: slow-growing economies are prevented from pursuing expansionary fiscal policies, while faster-growing economies are not constrained. This situation led to sustained nominal wage/price growth that was faster in peripheral countries than in core countries. The combination of faster-rising prices and nominal wages, and stronger domestic demand constrained deficit countries' exports, while stoking import demand; the reverse happened in surplus countries. In Germany, domestic demand was essentially stagnant and economic growth was driven solely by higher net exports. The widening competitiveness differentials until the crisis are shown in Figure 6.

The figure is presented in such a way (subtracting 2 per cent a year from the raw nominal unit labour cost figures) that a country keeping close to the x-axis would see domestic prices and unit wage costs growing in line with the ECB inflation target. France and Belgium are in this category. Germany and Austria experienced a marked increase in wage competitiveness (taking 1999 as a starting point) over the period, whereas the 'peripheral' economies, such as Ireland, Greece and Spain, lost competitiveness up to the crisis. Since 2009 there has been a sharp downward correction in the countries hit hardest by the crisis, without, however, a symmetric upward adjustment by the surplus countries, especially Germany.

11. For most purposes it is an acceptable simplification to equate current account (im)balances with trade imbalances. Deficits, then, arise when a country imports more goods and services than it exports; conversely, surpluses are the result of a country exporting more than it imports. Countries running persistent deficits incur net liabilities (foreign debts) vis-à-vis the rest of the world (or run down net asset positions accumulated in the past), while surplus countries build up net asset positions (or pay down past liabilities).

Figure 6 Nominal unit labour costs minus 2% p.a. (1999 = 100)



Source: AMECO data; authors' calculations.

4. Fiscal austerity against inclusive growth?

Having argued that the new economic governance and fiscal austerity in Europe as a response to the debt crisis pose a serious threat to any kind of output growth – and consequently to employment creation and recovery – we shall now look closer at the planned national measures for achieving the poverty headline target of the Europe 2020 Strategy. These measures have been announced in the context of the European Semesters every spring since 2012. We ask the following questions: do fiscal consolidation policies overshadow policies aimed at reducing poverty in its various guises? Are the policies planned in the context of

the European Semester mutually supportive and likely to increase cohesion across member states? And which objective is the EU's priority: consolidation of public finances or poverty reduction?

To answer these questions, we proceed as follows. Section 4.1 highlights how the EU countries have been doing in terms of poverty and social exclusion. Section 4.2 illustrates the extent to which the pressure for fiscal austerity is contradicting the inclusive growth paradigm and particularly its social component. This is done, first, by looking at the planned expenditure cuts – and particularly the cuts in social spending – that the countries report on in their Stability and Convergence Programmes. Second, we look at the emphasis of the Commission's country-specific recommendations as part of the policy cycle of the European Semester. Finally, we present some measures that were likely to have adverse implications for social inclusion and poverty from selected countries.

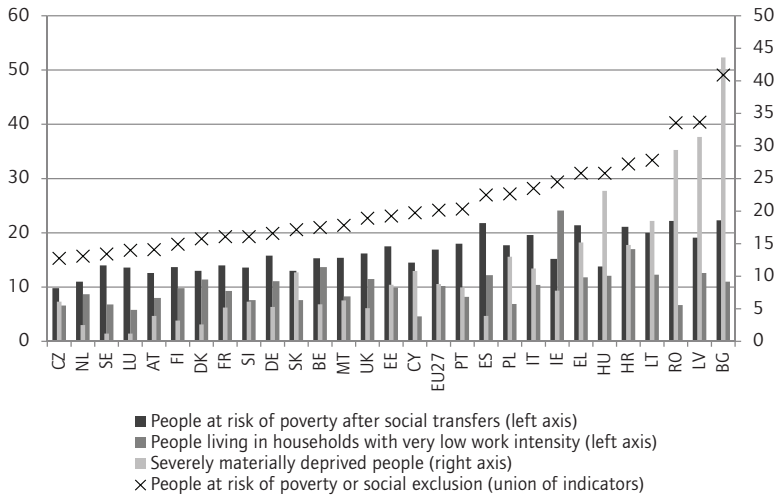
4.1 Poverty and social exclusion in the EU

Figure 7 shows how the EU countries were faring with regard to the overall EU headline target on poverty and social exclusion and its three component sub-indicators in 2011 (latest available data).¹² The overall target is composed of people who are at risk of poverty and/or suffering from severe material deprivation and/or living in households with very low work intensity.¹³ In most countries the 'at risk of poverty rate' best accounts for the observed poverty, as measured by the composite indicator. However, in the poorest countries – Bulgaria, Romania, Latvia and Hungary – 'severe material deprivation' is very pronounced, whereas it is of limited importance in most other countries. In Ireland, the most acute dimension of poverty is represented by 'low work intensity households'. The overall indicator capturing people at risk of poverty or social exclusion ranges from 15 per cent of the total population in the Czech Republic to 49 per cent in Bulgaria; the EU average was 24.2 per cent in 2011, one percentage point up from 2009. Eleven countries had more than one in four people (>25 per cent) in poverty according to the EU

12. It is important to keep in mind that the EU headline target refers to relative poverty, implying that poverty means very different things when comparing, for example, the Nordic and the central and eastern European countries. For comparative purposes and to stick with the European definition we will nevertheless use the EU headline target here.

13. The European Council (18 February 2011: 44–46) illustrates for all EU countries how the three groups overlap.

Figure 7 The overall EU headline target (people at risk of poverty or exclusion) and its three components, 2011 (share of total population)



Source: Eurostat, online database.

definition: (in ascending order) Spain, Poland, Italy, Ireland, Greece, Hungary, Croatia, Lithuania, Romania, Latvia and Bulgaria. The Nordic countries are doing particularly well and the continental European countries all perform above average. The Southern European countries exhibit below EU average performance but, with the exception of Greece, are not among the worst performers. The EU2 countries are by far worst performing and the new member states are spread over the whole distribution, with the Czech Republic being the best performer overall.

All countries (Greece, Portugal, Ireland, Latvia and Romania, Hungary, Spain and Cyprus)¹⁴ that are currently or have been recently in receipt

14. Latvia and Romania had to seek multilateral balance-of-payments assistance from, among others, the EU, the IMF, the World Bank and the EBRD in 2008 and 2009, respectively. To that end, they adopted conditionality programmes spelling out the structural reforms they had to undertake, all of which have been terminated by now. Hungary also received balance-of-payments assistance, although it stopped receiving it before the foreseen end. Greece, Ireland and Portugal had to seek financial assistance from the EU and the IMF in May 2010, December 2010 and May 2011, respectively, as their governments faced

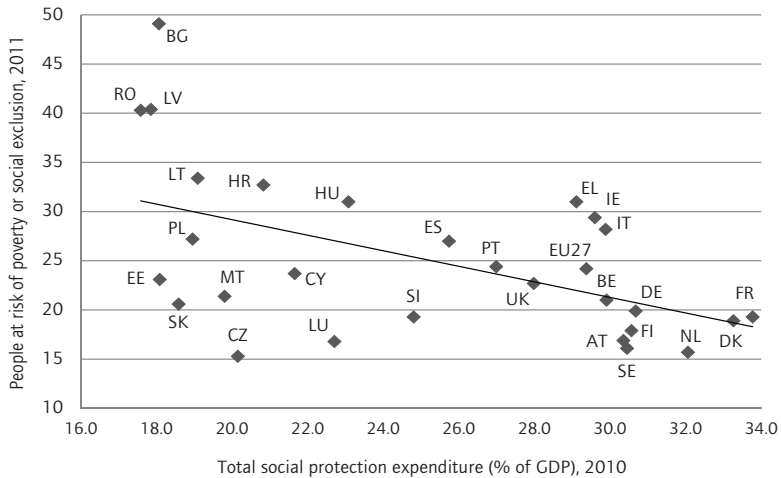
of financial assistance from the EU and the IMF and are thus under particular pressure to engage in rapid fiscal consolidation have poverty and social exclusion rates above or only slightly below (Cyprus) the EU average. The following sections will illustrate the negative impact of the pressure for fiscal austerity on the inclusive growth paradigm and point particularly to the danger of countries drifting apart.

4.2 Stability and convergence programmes against reforms to tackle poverty?

We examine first the plans announced by member states with regard to developments in public expenditure and, particularly, social payments in the context of their Stability and Growth programmes. To put the announced cuts into perspective, Figure 8 illustrates how the different member states are doing in terms of the level of total social expenditure as a share of GDP in 2010 (latest available data from Eurostat, and when shift to austerity policies took place) and the share of total population at risk of poverty or social exclusion in 2011. There is substantial variation in levels of social spending and associated risks of poverty and social exclusion. However, we see that in terms of social spending we can roughly distinguish two clusters of member states, namely the old and the new member states. Within these two clusters, there appears to be a negative correlation between social payments and the risk of poverty/social exclusion, which in fact is stronger among the new member states. In other words, the new member states, which are also significantly poorer on average than the old ones, have lower levels of total social spending as a share of GDP, while also presenting a wider variation of poverty risk, with some of the worst performers in the EU (Romania, Bulgaria, Latvia) but also the best performer (Czech Republic). In terms of the Europe 2020 Strategy, one would therefore expect that at least those member states with higher poverty risk rates would be called upon to make relatively more effort to increase social spending as a share of GDP in order to make progress towards their poverty headline target.

14. (*cont. from p. 315*) prohibitive borrowing costs in the financial markets, following rising concerns that they would not be able to carry on servicing their debt. Spain obtained financial assistance for recapitalising its banks in the summer of 2012, whereas the Cypriot government was bailed out in March 2013.

Figure 8 Comparison of levels of total social protection expenditure as a percentage of GDP and risk of poverty or social exclusion rate (% of population)

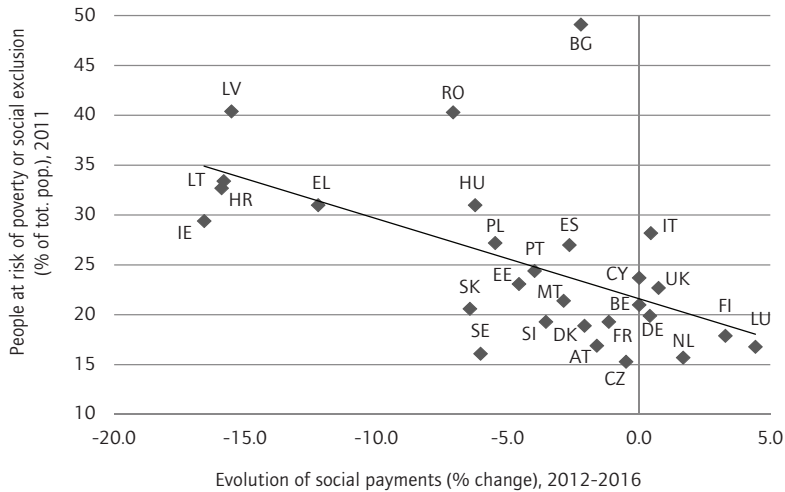


Source: Eurostat, online database.

Figure 9 presents the risk of poverty or social exclusion in 2011 and the planned evolution (percentage change) of social payments (including both money transfers and transfers in kind) as a proportion of GDP for 2012–2016, according to the Stability and Growth Programmes that were submitted in spring 2013 in the context of the European Semester (see Annex for complete tables on the development of total public expenditure and social payments).¹⁵ Cuts in social payments are envisaged in the majority of member states, although they are most severe in Ireland, Croatia, Lithuania, Latvia and Greece and also compara-

15. These figures are the only ones available for the current period and the near future. It should be noted that the Eurostat definition of social payments as used in Figure 8 is different to the one used for the purposes of Stability and Convergence Programmes (see Figures 9 and 10) in that the former includes all costs associated with a social policy programme (for example, administration costs), whereas the latter measures the payments themselves only. That results in a discrepancy in the size of social payments which is fairly large for some countries (such as Sweden, Denmark and Finland) but not others. However, we think that, given the absence of more recent Eurostat data and forecasts on these payments in the forthcoming years, this discrepancy does not affect the analysis.

Figure 9 Risk of poverty or social exclusion (2011) and planned evolution of social payments, 2012–2016



Source: National Stability and Growth Programmes, DG Ecfm and Eurostat online database.

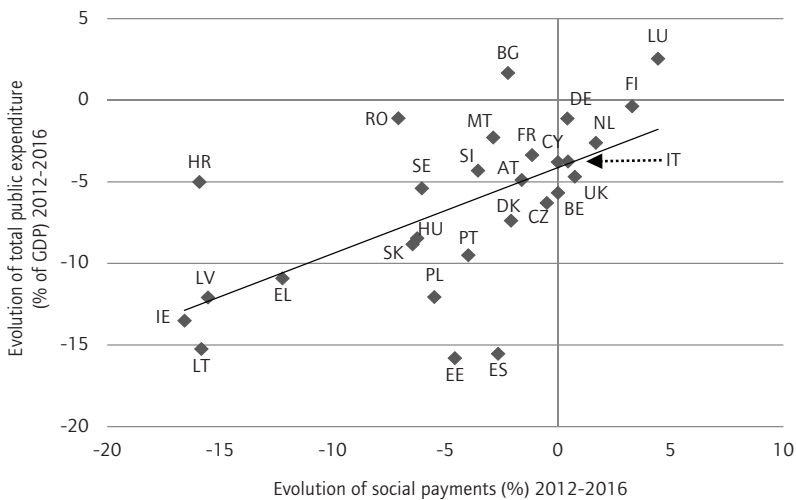
tively high in Romania, Slovakia, Hungary, Sweden and Poland. Except for Sweden and Slovakia these countries are among the ones with the highest proportion of the population at risk of poverty or exclusion. Ireland and Greece are currently under conditionality programmes for the financial help they have been receiving from the EU and/or the IMF and can thus be considered to have suffered a loss of policymaking autonomy. Lithuania was under pressure to demonstrate a commitment to sound public finances as it has been hoping to adopt the euro since 2007.¹⁶ Interestingly, Romania, Sweden, Latvia, Lithuania, Slovakia and Poland have all had and are projected to have public debt to GDP ratios well below the 60 per cent that the Stability and Growth Pact stipulates. This implies that there are few fundamental concerns about the

16. Countries giving up their currency and monetary policy tools become vulnerable to financial markets' beliefs about their capacity to carry on servicing their public debt, as they lose control over their central bank. As the current crisis has shown, a market belief that a government cannot carry on servicing its debt can become a self-fulfilling prophecy, once market participants start requiring a higher interest rate in order to continue lending money to the government. See (DeGrauwe 2011b).

sustainability of their public finances. With the exception of Sweden, and to some degree also Slovakia, there are certainly concerns about the social exclusion of particular groups within their populations, however, and the planned cuts in social payments risk aggravating the situation. Overall, the positive correlation between the extent of poverty/social exclusion and the extent of the planned retrenchment of social spending is profoundly worrying and completely at odds with the EU poverty headline target.

To what extent are these planned social cuts in line with more general cuts in public expenditure and how much do they reflect a planned rolling back of the welfare state alone? Figure 10 shows how the planned evolution of social expenditure compares with the planned evolution of public spending between 2012 and 2016 according to the Stability and Growth programmes of 2013. A couple of points stand out. First, the retreat of the welfare state within the framework of public spending retrenchment is severest in Romania and Croatia and also comparatively high in Luxembourg, Latvia, Malta, Ireland, Greece and Sweden. Secondly, the retreat of the state and of the welfare state is more

Figure 10 Evolution of public and social expenditure, 2012–2016 (%)



Source: National Stability and Growth Programmes, DG Ecfm.

pronounced in some of the member states whose populations are at relatively high risk of poverty, such as Latvia, Lithuania, Greece and Ireland.

The picture that emerges from these data is that the countries making disproportionate cuts are those that are already doing comparatively badly in terms of poverty and social exclusion. More specifically, especially in those countries in which the EU has had a say in how much the state could spend and what issues it should be focussing on within the framework of financial aid programmes, there has been a rolling back of both public expenditure and social payments.

4.3 EU priorities: predominance of fiscal issues in the country-specific recommendations

Under the impact of the economic crisis on public finances, the alignment of macroeconomic reporting (Stability and Convergence Programmes) and reporting on structural reforms (National Reform Programmes) in the context of the European Semester has to some extent overshadowed the Europe 2020 targets and particularly the inclusive growth agenda. Countries are supposed to give priority to macro-fiscal issues (compare, for example, European Commission 2010c; 2012b). This is expressed, for example, in the 2013 Annual Growth Survey which, as we have seen, is primarily fiscal in orientation, combined with a neoliberal supply-side reform agenda.

The same predominance of fiscal consolidation is evident when looking at the next step in the European Semester, on which we focus in this section: the drawing up of country-specific recommendations based on the submission of the Stability and Convergence and the National Reform Programmes (NRPs). On the basis of the Stability and Convergence Programmes and the NRPs, country-specific recommendations are issued by the European Commission and must be approved by the European Council.¹⁷

17. Country-specific recommendations as well as national reform programmes and stability programmes can be found here:
http://ec.europa.eu/europe2020/making-it-happen/country-specific-recommendations/index_en.htm

What do these recommendations reveal about the relative priority of fiscal consolidation – as pursued in the context of new economic governance and policies to deal with the debt crisis – over policies to tackle poverty? A first interesting point is that the countries in receipt of financial assistance from the EU and the IMF have not been receiving specific recommendations from the European Commission but have instead been called upon to implement the measures laid down in their respective memoranda of understanding. At most, these memos contain general clauses stipulating that the most vulnerable segments of the population should be shielded from the impact of the fiscal consolidation measures. However, the specificity of actions to that end does not parallel those of reducing budget deficits, while measures of a more positive nature that could actively help to reduce poverty are not mentioned at all (see, for example, European Commission 2011; Ministry of Finance-Hellenic Republic 2011; Portuguese Ministry of Finance and Public Administration 2011). On the contrary, minimum wage cuts were effected in Greece and initially in Ireland, too, although in the latter they were rolled back a few months later. Last but not least, in plans for reforming pension and social security systems, 'sustainability' clearly takes precedence over adequacy of benefits; in fact, the latter is often simply not considered.

For 2013, each of the remaining 23 countries received a recommendation on budgetary discipline (always the first recommendation), whereas the remainder of the recommendations vary considerably in content. As regards the Europe 2020 priority of inclusive growth, labour market inclusion clearly predominates over wider poverty prevention goals. All 23 countries – and among them the three countries with the highest employment rates – received recommendations on improving labour market participation, with particular emphasis on enhancing the participation of older workers, promoting active ageing and lifelong learning and providing a 'youth guarantee'. Recommendations on education and training were issued to 22 countries, recommendations on active labour market policies to 20 and recommendations on pensions to another 14; again, incentives for labour market participation stand centre-stage (for example, enhancing participation of older workers, promoting active ageing and lifelong learning and reducing early retirement and increasing the effective retirement age). With regard to social protection systems, social services and social assistance, adequacy is also mentioned in a number of cases. Seven countries received recommendations on wages (with an emphasis on aligning wage growth and productivity) and eighteen on public services, in most cases with a focus on improving effectiveness.

A number of these measures may be helpful in fighting poverty and social exclusion, but they are more likely to work when job creation is buoyant and some redistribution policies are in place. Only nine countries received recommendations on poverty and social exclusion, namely Belgium, Bulgaria, Spain, Hungary, Lithuania, Latvia, Poland, Romania and the United Kingdom.¹⁸ As laid out in Section 3.1 member states are allowed to use different indicators to report on poverty, and the respective sections in the NRPs thus vary substantially in content and length. This is likely to have rendered the process of issuing recommendations on poverty more difficult.

All five recommendations to the euro area countries, which receive specific recommendations from the Commission, focused in 2013 on macroeconomic issues (aggregate macroeconomic policy stance, fiscal policy differentiation, differences in lending rates to SMEs across member states, the repair of banks' balance sheets, coordination of economic reforms, especially in the labour and product markets) (compare Council of the European Union 2013). The accompanying, more detailed document (European Commission 2013) does not contain a single reference to inclusive growth and the detailed table entitled 'Labour market and social indicators' provides figures on labour productivity and unit labour cost growth instead of the poverty and social inclusion indicators.

To wrap up, at the level of the country-specific and euro-area recommendations, not only do the outcomes of macroeconomic prescriptions risk running counter to the coordination related to smart, sustainable and inclusive growth, but the inclusive growth paradigm – where it is referenced – seems to be strongly driven by a desire to boost labour force participation, largely based on making-work-pay strategies that are of dubious value in a context of unemployment caused primarily by a shortfall of aggregate demand.

4.4 Evidence from the fiscal austerity packages

To underpin our argument, in this section we have used evidence from national experts (Theodoropoulou and Watt 2011) and other sources

18. The recommendations to Hungary and the Netherlands are only indirectly linked to the poverty headline target, emphasising tailor-made programmes to low skilled and other disadvantaged groups and the labour market integration of vulnerable groups.

on the austerity programmes adopted by late 2010/early 2011 in 17 EU member states to obtain insights into their effects on poverty and social inclusion (on austerity measures and their social impacts, see also the individual chapters of this volume).

Indirect tax hikes, which tend to disproportionately affect those at the low end of the income distribution, were reported in several countries (Poland, Hungary, Estonia, Cyprus and Latvia), most of them at the higher end of the poverty distribution within the EU. Indeed, the EU recommendations state that tax increases, wherever necessary, should focus more on indirect taxes as these are less likely to interfere with employment creation (European Commission 2010b; European Commission 2012a). Nonetheless, some countries (France, Austria, Luxembourg and the United Kingdom under the previous Labour administration) increased progressive taxes (income and wealth taxes). Heise and Lierse (2011), who assess the impact of austerity measures on the European social model for seven European countries, also come to the conclusion that in all these countries the economic crisis and the resulting public debt have been used as excuses for social cuts which in most countries hit low earners disproportionately.

The young working under precarious employment contracts are particularly hard hit in Italy due to the limited coverage of unemployment insurance. The unemployment rate for those under 25 in Italy stood at 27.8 per cent in 2010 (Eurostat LFS data), more than three times higher than the average, which was 8.4 per cent (Theodoropoulou and Watt 2011). This implies a concentration of social exclusion in this group.

In a similar vein, in Greece (for details, see Matsaganis and Leventi 2011), because of their very low coverage by unemployment insurance, the unemployed have been particularly affected by the fiscal austerity programme that is a condition of the financial support the country receives from the EU and the IMF. Pensioners have also been targeted. Indirect tax increases have been regressive. Some measures, however, such as some elements of public sector retrenchment, have tended to narrow the income distribution (Matsaganis and Leventi 2011). Overall, as a result of the austerity and the wider recession, 5 per cent of the Greek population saw their 2010 incomes fall below the 2009 poverty line, swelling the ranks of those who were already in poverty (another 20 per cent of the population). However, while the crisis has raised demand for social protection, the supply of social benefits has been reduced rather than increased.

Social benefit recipients have been adversely affected by cuts in Latvia, Romania, Germany, the United Kingdom, Spain and Ireland (Heise and Lierse 2011: 24–26). In Portugal, the recipients of non-contributory benefits (social assistance, which is more likely to be received by people at the margins of the labour market) are likely to suffer most from measures to reduce expenditure on these benefits within the framework of the programme imposed as a quid pro quo for financial support from the EU and the IMF (Portuguese Ministry of Finance and Public Administration 2011). Again, it is worth noting that the majority of these countries are at the upper end of poverty distribution in the EU, and have also been finding it hard to finance their public debt in the markets.

5. Conclusion

Europe is currently going through the worst economic crisis of the post-War era. Unemployment has increased dramatically in several countries, especially among young people, and the prospects for output growth recovery appear gloomy for the next few years. Due to the economic interdependence of EU member states, these developments are likely to spread across the Union and especially within the euro zone. Past experience shows that this combination of high unemployment and prolonged weak output growth is bound to lead to persistently high unemployment, the depreciation of skills and the labour market detachment of unemployed people. The social consequences of these developments will be grave as social exclusion is likely to increase.

Against this background, we have sought to evaluate the coherence of the policy responses promoted at the EU level in response to the crisis and the quest for growth. We have investigated whether the pursuit of fiscal austerity as dictated in the context of the European Semester runs counter to the pursuit of inclusive growth through reducing poverty, which is one of the priorities of the Europe 2020 Strategy. Our answer is affirmative and our argument is spelled out along two axes.

First, the underlying principles of the proposed new economic governance structures are bound to impose a fiscal austerity bias which, under the current circumstances, will inevitably lead to depressed demand and no output growth in the short, medium and, due to hysteresis mechanisms, eventually the long term. This is inimical to growth as such, but is also expected to make any growth that is achieved less inclusive.

Secondly, a closer look at the recommendations to member states and their declared stability and convergence programmes suggests that all policy considerations with regard to tackling poverty and social exclusion are subjugated to fiscal consolidation and other goals. It is not the first time that inclusive growth has been subordinated to other issues, such as macroeconomic concerns, productivity and employment growth, but the crisis and the subsequent austerity measures have further emphasised these tendencies. This predominance of public finance concerns over inclusive growth is particularly striking in the cases of member states that have been performing below the average in terms of poverty and social exclusion, but have no particular problems in terms of the sustainability of their public finances. To that end, we have also provided some evidence from austerity packages already adopted in selected member states (as available) and how they have been adversely affecting vulnerable groups or doing little to improve their position. The crisis could and should have been used as an opportunity to introduce corrections to the previous growth model, of which rising inequality was a prominent feature (Watt 2009). However, the evidence suggests not only that this has not happened, but that current policies are tending to exacerbate the direct negative effects on distribution and poverty/exclusion arising from the crisis itself.

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Annex

Table 1 Evolution of total public expenditure 2012–2016, according to Stability and Growth Programmes 2011 (% of GDP)

	2012	2013	2014	2015	2016	2016– 2012 (p.p.)	2016– 2012 (%)
EE	40.5	39.9	37.3	35.3	34.1	–6.4	–15.8
ES	47	43.3	42.3	41.2	39.7	–7.3	–15.5
LT	36.1	34.7	33.7	32	30.6	–5.5	–15.2
IE	42.2	42.5	39.6	37.5	36.5	–5.7	–13.5
LV	36.4	36.3	34.7	31.9	32	–4.4	–12.1
PL	42.3	41.3	40.5	38.9	37.2	–5.1	–12.1
EL	50.4	47.4	46.9	46.4	44.9	–5.5	–10.9
PT	47.4	48.1	46.2	44.2	42.9	–4.5	–9.5
SK	37.4	37	35.2	33.8	34.1	–3.3	–8.8
HU	48.5	49.6	49.8	49	44.4	–4.1	–8.5
DK	58.3	56.7	55.9	54.9	54	–4.3	–7.4
CZ	44.5	43.3	43	42.3	41.7	–2.8	–6.3
BE	54.7	53.8	53	52.2	51.6	–3.1	–5.7
SE	51.9	52.5	51.8	50.4	49.1	–2.8	–5.4
HR		42	41.3	40.8	39.9	39.9	–5.0
AT	51.2	51.3	50.4	49.4	48.7	–2.5	–4.9
UK	44.9	43.2	44.9	43.8	42.8	–2.1	–4.7
SI	48.8	53.4	49.4	47.9	46.7	–2.1	–4.3
CY	42.3	43.7	44.2	42.6	40.7	–1.6	–3.8
IT	50.7	51.1	49.8	49.4	48.8	–1.9	–3.7
FR	56.6	56.9	56.4	55.5	54.7	–1.9	–3.4
NL	50	49.9	50.4	48.9	48.7	–1.3	–2.6
MT	43.9	44.9	44.9	44.9	42.9	–1	–2.3
DE	45	45.5	44.5	44.5	44.5	–0.5	–1.1
RO	36.4	36.2	36.1	36.2	36	–0.4	–1.1
FI	55.7	56.3	56.1	55.6	55.5	–0.2	–0.4
BG	35.7	38.5	37.8	37.5	36.3	0.6	1.7
LU	43	43.3	43.3	43.8	44.1	1.1	2.6

Source: National Stability and Growth Programmes. DG Ecfm.

Table 2 Evolution of social payments 2012–2016, according to Stability and Growth Programmes 2011 (% of GDP)

	2012	2013	2014	2015	2016	2016– 2012 (p.p.)	2016– 2012 (%)
IE	17.5	16.8	16	15.1	14.6	–2.9	–16.6
HR	17.6	16.8	16.2	15.5	14.8	–2.8	–15.9
LT	13.9	13.3	12.6	12.1	11.7	–2.2	–15.8
LV	10.3	10.4	9.8	9.4	8.7	–1.6	–15.5
EL	22.9	21.3	21.1	20.8	20.1	–2.8	–12.2
RO	12.7	12.2	12.2	12	11.8	–0.9	–7.1
SK	18.6	18.4	17.9	17.6	17.4	–1.2	–6.5
HU	17.6	17.5	17	16.8	16.5	–1.1	–6.3
SE	18.2	18.3	17.9	17.5	17.1	–1.1	–6.0
PL	16.4	16.4	16.2	15.9	15.5	–0.9	–5.5
EE	13.1	12.9	12.7	12.7	12.5	–0.6	–4.6
PT	22.6	23.9	22.7	22.1	21.7	–0.9	–4.0
SI	19.7	20.2	20	19.6	19	–0.7	–3.6
MT	13.9	13.7	13.7	13.7	13.5	–0.4	–2.9
ES	18.8	18.9	18.9	18.6	18.3	–0.5	–2.7
BG	13.5	14.2	14.1	13.7	13.2	–0.3	–2.2
DK	19.2	19.5	19.3	19.2	18.8	–0.4	–2.1
AT	24.8	25	24.8	24.6	24.4	–0.4	–1.6
FR	26	26.4	26.3	25.9	25.7	–0.3	–1.2
CZ	20	20.2	20.3	20.2	19.9	–0.1	–0.5
BE	25.8	26.3	26.1	25.9	25.8	0	0.0
CY	15	15.7	16.3	15.8	15	0	0.0
DE	24.4	24.5	24.5	24.5	24.5	0.1	0.4
IT	22.6	23.1	23	22.9	22.7	0.1	0.4
UK	13.5	14.1	13.9	13.7	13.6	0.1	0.7
NL	23.8	23.8	24	24.2	24.2	0.4	1.7
FI	21.3	21.8	21.9	21.9	22	0.7	3.3
LU	20.3	20.7	20.8	21	21.2	0.9	4.4

Source: National Stability and Growth Programmes. DG Ecfm.

European economic governance and its intervention in national wage development and collective bargaining

Thorsten Schulten and Torsten Müller¹

1. Introduction

The European system of economic governance, set up over a period by the EU and its member states in order to cope with the crisis, represents a new model of European politics that can be described as a new European interventionism. This new approach is characterised by three key features. First, it stands for an increasingly authoritarian top-down approach, with the European level directly determining national-level policies, even in policy areas such as wages and collective bargaining, in which the EU has no formal competences. The second key characteristic of the new European interventionism is the strengthening of the European executive organs – in other words, the European Commission and the European Council – vis-à-vis parliaments both at European and at national level (Oberndorfer 2013a). And the third is its one-sided focus on fiscal austerity and cost competitiveness, which considers wages – or, more specifically, downward wage flexibility – to be the main adjustment mechanism for the current macroeconomic imbalances.

As a consequence, the establishment of the new system of European economic governance enabled European institutions such as the European Commission, the European Central Bank (ECB) and the European Council to intervene directly in national collective bargaining arrangements by pushing for wage cuts and freezes and the decentralisation of wage setting arrangements. The new system of European economic governance therefore marks a paradigm shift in the EU's approach to collective bargaining, from the acceptance of free collective bargaining to direct political intervention in national bargaining outcomes and procedures.

1. This chapter is a revised and updated version of Schulten and Müller (2013).

The objective of this chapter is to trace this paradigm shift and its implications for wage development and national collective bargaining arrangements. Section 2 gives a brief overview of the development of the new system of economic governance and illustrates how European policy, step by step, tightened its grip on national wage policies and wage-setting arrangements. Based on an analysis of the underlying political and economic rationale of the new interventionist approach, Section 3 describes the various tools of intervention, in terms of both their procedural characteristics and their content. Section 4 represents the empirical core of this chapter and looks at the key areas of supranational political intervention in national wage policies: the public sector and minimum wages; the decentralisation of multi-employer bargaining arrangements; and, finally, the impact of all these interventions on the overall pattern of wage development. The concluding Section 5 discusses the future of a European wage policy and the strategic options available to trade unions if they wish to counter the current strategy of European interventionism.

2. The role of wage policy under the new European economic governance

According to the Treaty on the Functioning of the European Union (TFEU, Article 153.5), it is explicitly ruled out that the EU shall be granted any competences in the area of wage policy. This provision was introduced for the first time in 1991, with the so-called Social Protocol of the Maastricht Treaty. Later on it became part of the Social Chapter of the Amsterdam Treaty of 1997. Paradoxically, the exclusion of wage policy from the realm of EU competences was introduced at the same time as the decision to launch the European Monetary Union (EMU). The latter has led not only to a new stage of European economic integration, but has also created a new macroeconomic regime which has set new terms and challenges for national wage policies (Hein *et al.* 2005).

The existing legal framework, however, has never prevented EU institutions such as the European Commission, the ECB or even the European Council from making general statements and recommendations about wage policy. The Broad Economic Policy Guidelines (BEPG), for example, which have been regularly drafted by the Commission and adopted by the Council since 1993, have always included demands for more moderate and more dispersed wage developments (Hein and

Niechoj 2007). Moreover, the so-called Macroeconomic Dialogue was established in 1999 as a forum for exchanges of views between the Council, the Commission, the ECB and the European employers' and trade union organisations, aiming at a 'coordination of economic policy and improvement of mutually supportive interaction between *wage developments* and monetary, budget and fiscal policy' (European Council 1999; authors' emphasis). Finally, it has been the European trade unions, in particular, which since the late 1990s have continually emphasised the need for European coordination of collective bargaining in order to prevent downward wage competition in Europe (Schulten 2002, 2003).

While these early European initiatives in the area of wage policy shaped a certain political and economic discourse at EU-level, they have never led to legally binding policy initiatives. If at all, they have had only very limited impact on the practice of wage policy, which remains almost exclusively the result of national wage-setting institutions. However, the situation started to change fundamentally with the emergence of the so-called 'new European economic governance'. The latter encompasses a set of new policy rules and procedures that have been developed in the wake of the economic crisis that hit in 2008 and which are intended to achieve a more binding European coordination of economic policy (Deryse 2012).

A new system of European economic governance began to emerge in 2010 with the adoption of the 'Europe 2020' strategy, which included the introduction of the so-called 'European Semester' as a yearly cycle of European economic policy coordination. Every year the EU issues policy recommendations for all EU member states on the basis of a detailed economic analysis. These recommendations must then be transposed into national 'reform programmes', whose effectiveness will again be assessed by the EU.

The annual economic coordination cycle was further developed in 2011 with the adoption of a package of five Regulations and one Directive. The so-called 'Six-Pack' contains two new major instruments intended to intensify economic policy coordination: one is the establishment of a new system of enhanced fiscal and macroeconomic surveillance through an alert mechanism for the early detection of macroeconomic imbalances based on a 'scoreboard' of economic indicators. The second is the introduction of an automatic procedure for imposing financial sanctions on those countries that fail to comply with the policy recommendations

issued on the basis of the alert system. As a consequence, the European policy recommendations for member states lose their purely voluntary character and reach a much higher degree of liability.

Wage policy plays a prominent role within the new system of European economic governance. This was underlined, in particular, by the adoption of the Euro Plus Pact in 2011, which defines wages explicitly as the main economic adjustment variable for overcoming economic imbalances and fostering competitiveness. Consequently, the Euro Plus Pact calls for close monitoring of wages and wage-setting institutions at European level (European Council 2011). Moreover, the new 'scoreboard' of economic indicators that have to be considered by the EU member states explicitly includes unit labour costs and defines a certain margin for 'permitted' wage and labour costs developments. Currently, all countries within the euro zone are allowed a maximum 9 per cent increase in unit labour costs over a period of three years (12 per cent for EU countries outside the euro zone) (European Commission 2012a).

As a result of the new European economic governance, the EU's influence on national wage policies has grown substantially, especially since EU policy recommendations have become more binding because member states that ignore them face financial sanctions. The possible scope of the new European interventionism in the area of wage policies becomes most obvious in those crisis-ridden countries that rely on financial assistance from the EU and/or the International Monetary Fund (IMF). In exchange for new credits, these countries have had to introduce far-reaching policy reforms, which were laid down either in so-called 'Memorandums of Understanding' with the 'Troika' comprising the European Commission, the ECB and the IMF (in the case of Cyprus, Greece, Ireland and Portugal) or in 'Stand-By Arrangements' with the IMF (in the case of Hungary, Latvia and Romania). The policy measures that these countries had to agree to included far-reaching labour market reforms, such as changes in wage development and collective bargaining systems.²

Strong European intervention was also felt in Spain, which received international financial aid for its financial sector. Although this rescue plan is not for the complete economy, it has been linked with a Memorandum

2. For an overview of the broad range of labour market reforms imposed by the Troika or the IMF in the various European countries see: Clauwaert and Schömann (2012) and Hermann (2013).

of Understanding in which the Spanish government had to commit itself 'to implement the country-specific recommendations in the context of the European Semester', including more fundamental changes in labour market regulation (European Commission 2012b). Before that, it was the ECB that practiced a more 'unofficial' form of intervention by making the purchase of government bonds conditional on policy reforms. The same holds true for Italy, where in autumn 2011 a confidential letter from the top of the ECB was leaked to the public, in which the Italian government was asked to carry out far-reaching structural reforms, including the radical decentralisation of collective bargaining (Meardi 2014; for the letter see: Draghi and Trichet 2011). Since autumn 2012, this kind of policy has become more official after the ECB announced that it would buy state bonds without limit if the affected countries agree to certain policy reforms.

Following the proposals made by the European Commission (2012c) for a 'deep and genuine economic and monetary union', as well as by German Chancellor Angela Merkel (2013), the next step in the development of the new European economic governance would be the conclusion of competitiveness pacts between the EU and the member states, in which the latter commit themselves to implement 'structural reforms', which include wage policy and collective bargaining. Following the logic of the Memorandums of Understanding, this new system of competitiveness pacts has been rightly labelled 'Troika for everyone' (Oberndorfer 2013b) and would transpose current practices in bailout countries to the EU as a whole. Even though the initiative to conclude competitiveness pacts was blocked at the meeting of the European Council in December 2013, the principal idea remains on the political agenda of the newly appointed Commission (Oberndorfer 2014).

3. European intervention in national wage policies

There are at least three main sets of arguments that serve as legitimisation for European interventions in the area of wage policies. Two are at a more macro level and reflect the dominant perception of the current crisis in the EU as a debt crisis and a crisis of competitiveness. First of all, the EU argues in favour of a strong austerity policy in order to overcome the debt crisis. This view became even more pronounced with the adoption of the Fiscal Pact in March 2012, which can be interpreted as an attempt to make the austerity approach irreversible (Konecny 2012:

389). Austerity policy always has an immediate impact on wage policy as labour costs in the public sector often represent a significant part of public budgets. Thus, all current austerity programmes include demands for cuts and freezes of public sector wages.

Secondly, the growing economic imbalances between the so-called ‘surplus’ and ‘deficit’ countries in Europe are understood to be the result of diverging developments in national competitiveness, caused mainly by diverging trends in wages and unit labour costs. Before the creation of EMU, deficit countries would have solved their competitiveness problems by devaluating their national currency. Because within EMU this is of course no longer possible, the less competitive countries need a policy of ‘internal devaluation’, which involves increasing competitiveness by reducing labour costs, which is thus understood as a ‘functional substitute to currency devaluation’ (Armington and Baccaro 2012: 256). For the ECB, one of the ‘main policy conclusions’ of its 2012 report ‘Euro area labour markets and the crisis’ is that ‘downward wage rigidities are an impediment to restoring competitiveness (and thus employment), particularly in those euro area countries that had accumulated external imbalances before the crisis’ (ECB 2012: 9). While currently the dominant view in the EU is to put the whole burden of rebalancing on the deficit countries, there is also a more Keynesian variant of this argument that states that the surplus countries (in particular, Germany) should play a stronger role by promoting stronger wage growth (for example, Grauwe 2012; Malliaropoulos and Zarkos 2013). Both views, however, focus on wages as the core – or sometimes even only – adjustment variable in the EMU.

There is a third set of more micro-oriented arguments that have regained prominence against the background of the sharp increase in unemployment in many European states. These arguments are based on the neo-classical view that unemployment is mainly the result of institutional ‘rigidities’ in the labour market. A perfect example of this view was presented in the DG ECFIN Report ‘Labour Market Developments in Europe 2012’, which presented a long list of so-called ‘employment-friendly reforms’. Apart from various issues of labour market deregulation – for example, cutting unemployment assistance, reducing employment protection and increasing the retirement age – the list also includes a subsection on the ‘wage bargaining framework’, which demands that member states do the following:

- ‘decrease statutory and contractual minimum wages’;
- ‘decrease bargaining coverage’;
- ‘decrease (automatic) extension of collective agreements’;
- ‘reform the bargaining system in a less centralised way, for instance by removing or limiting the “favourability principle”’;
- introduce/extend ‘the possibility to derogate from higher level agreements or to negotiate firm-level agreements’;
- promote measures that ‘result in an overall reduction in the wage setting power of trade unions’ (European Commission 2012d: 103–104).

Considering the international research on the macroeconomic performance of different collective bargaining systems,³ DG ECFIN has rightly acknowledged in another paper that ‘there is no strong evidence in support of a single superior wage setting model’ (European Commission 2011: 17). Nevertheless, in its policy recommendations, DG ECFIN always takes a decentralised, company-based bargaining system as the benchmark, because this system seems to allow companies to adjust better to varying economic developments. Regarding this point, the Commission received support from the Euro Plus Pact, which calls on member states, somewhat convolutedly, to ‘review the wage setting arrangements, and, where necessary, the degree of centralisation in the bargaining process’ (European Council 2011: 16).

Moving from analysing the underlying rationale to assessing the practice of EU intervention in wage policy, it should be noted that in recent years 19 out of 28 EU member states have been affected by at least some EU initiatives (see Table 1). For the EU there are two main channels of intervention, which vary in the extent to which they are binding. The first channel relies on the country-specific recommendations issued within the framework of the European Semester. Even though these recommendations are not legally binding, in combination with the new alert mechanism, which includes the possibility of financial sanctions, they might become more binding in future. The second channel relies on the quid pro quo of reforms for financial support. Because the wage policy measures are laid down in agreements between the Troika or the IMF and national governments, this second channel of political intervention has a more immediate impact and is therefore more binding in character.

3. See, for example, Aidt and Tzannatos (2008) and Traxler and Brandl (2011).

Table 1 European interventionism in the area of wage policy, 2011–2014

Recommendations/agreements:	Addressed countries:
1. Country-specific recommendations within the framework of the European Semester:	
Decentralisation of collective bargaining	Belgium, Italy, Spain
Reform/abolition of automatic wage indexation	Belgium, Cyprus, Luxembourg, Malta
Moderation of minimum wage development	France, Portugal, Slovenia
Moderation of general wage development/ nominal wages in line with real productivity	Belgium, Bulgaria, Croatia, Finland, Italy, Slovenia, Spain
Wage development in line with productivity growth / to support domestic demand	Germany
Addressing high wages at the lower end of the wage scale	Sweden
2. Country-specific agreements between EU-ECB-IMF or IMF and national governments within the framework of Memorandums of understanding:	
Decentralisation of collective bargaining	Greece, Portugal, Romania
More restrictive criteria for extension of collec- tive agreements	Greece, Portugal, Romania
Reduction/freeze of minimum wages	Greece, Ireland, Latvia, Portugal, Romania
Reduction/freeze of public sector wages	Greece, Hungary, Ireland, Latvia, Portugal, Romania
Wage freezes in private sector	Greece
Nominal wage development in line with real productivity	Cyprus, Portugal
No recommendations in the area of wage policy:	
Austria, Czech Republic, Denmark, Estonia, Lithuania, Netherlands, Poland, Slovakia, United King- dom	

Source: Authors' compilation on the basis EU 2020 country-specific recommendations for 2011–2014 (available from the EU web page: http://ec.europa.eu/europe2020/index_en.htm) and the 'Memorandum of Understanding' between EU-ECB-IMF or IMF and national governments (available from the IMF web page: <http://www.imf.org>).

However, the demands for certain measures usually come from the Troika, which insists on their implementation as a precondition for financial assistance. Therefore, one can say that in practice many national initiatives in the area of wage policy have often been 'imposed' by the Troika.

For most countries, however, the EU's attempts to influence national wage policies have up to now been limited to (non-binding) country-specific recommendations within the framework of the European Semester. So far, the EU has used these instruments for 13 member states. In many

cases, the recommendations have been relatively vague, calling for moderate development of wages in general (Bulgaria, Finland, Italy, Slovenia and Spain) or of minimum wages in particular (France, Slovenia and Portugal). While in the case of Sweden the EU *de facto* demanded an extension of the low wage sector, in the case of Germany it called for wage development to remain in line with productivity growth, which can be understood as a plea for a somewhat higher wage growth. In 2014, a further three countries (Belgium, Croatia and Italy) received the recommendation to ensure that wages stay in line with productivity, with the opposite intention of ensuring moderate wage increases, because the EU Commission demands that nominal wages should follow real productivity without any compensation for inflation.

Much more precise recommendations have been given regarding the reform of wage-setting systems. In the case of Belgium, Italy and Spain, the EU has asked for a decentralisation of collective bargaining by making it easier for companies to derogate from multi-employer agreements. Finally, Belgium, Cyprus, Luxembourg and Malta are strongly criticised as the only countries in the EU that still have a national system of automatic wage indexation (Mongourdin-Denoix and Wolf 2010). Here the EU has demanded, if not the abolition, at least a fundamental reform of these systems in order to make indexation less strict and binding.

The second, more binding channel of political intervention has been applied to seven states that have been under international bailout programmes (Cyprus, Greece, Hungary, Ireland, Latvia, Portugal and Romania). In all seven cases, EU interventions affected both the current development of wages and the structure of collective bargaining. In addition, the Troika has made explicit reference to the country-specific recommendations developed within the framework of the European Semester with respect to Spain.

In terms of content, the Troika first of all demanded significant cuts and subsequently freezes of public sector wages in order to reduce public deficits. Furthermore, the Troika has called for cuts (in the case of Greece and Ireland) or freezes (in the case of Latvia, Portugal and Romania) of national minimum wages. Both measures were also intended to have a dampening effect on wage developments in the private sector. However, in the case of Greece, the Troika has even called for a freeze of seniority allowances in private collective agreements. Finally, in Greece, Portugal and Romania (as well as Spain) the Troika has pushed for essential

changes in the national wage-setting systems, aiming at a radical decentralisation of collective bargaining and a sharp restriction of the criteria for extending collective agreements.

4. Impact of the new European interventionism on recent developments in national wage policies

In the wake of the current crisis, the emergence of a new European interventionism has already shaped the development of national wage policies in many European countries, and in particular in those countries that are currently under the economic surveillance of the Troika. Here, international pressure has also fostered the development of a new state interventionism at national level, which in every case has included the same measures: pay cuts or freezes in the public sector, a restrictive minimum wage policy and the fundamental reconstruction of the collective bargaining system, leading to a radical decentralisation or even dismantling of multi-employer bargaining. The objective of the present section is to analyse in more detail the concrete implications of the new European interventionism in the three above-mentioned areas. Because the impact on public sector wages and the decentralisation of collective bargaining systems has been particularly pronounced in the countries under international economic surveillance, the key focus of the respective sub-sections is these eight countries. The sub-sections on minimum wages and real wage developments open the perspective to the whole of Europe in order to illustrate the broader impact of European interventionism on wage developments in Europe more generally.

4.1 Cuts and freezes of public sector wages

Public sector pay cuts and freezes have been one of the main tools of direct intervention used by national governments in an effort to reduce public spending in order to stabilise government finances and to 'reassure' bond markets (ILO 2013: 20). Public sector wages are an easy target for direct political intervention because in many European countries the salaries of public sector employees are regulated not by collective agreements but by law, thus enabling governments to impose pay cuts and freezes unilaterally. Direct intervention in public sector wages was furthermore given additional legitimacy by the Euro Plus Pact,

which emphasises the wage-leadership function of public sector wages in many countries, and therefore explicitly calls on the EU member states to ‘ensure that wages settlements in the public sector support the competitiveness efforts in the private sector’ (European Council 2011: 16).

Recent analyses of public sector wage developments during the crisis identify the following key tendencies (Glassner and Keune 2012; Grimshaw *et al.* 2012, ILO 2013, LRD 2012). First, wage cuts and freezes have by no means been restricted to those countries hit particularly hard by the crisis. Between 2008 and 2012, public sector pay reforms were adopted by at least 18 out of the 27 EU Member States. The fact that pay cuts and/or freezes were also imposed in countries that are characterised by a comparatively low level of debt (such as the Czech Republic), or that have remained relatively unaffected by the crisis (such as Poland) suggests that, in some countries, the crisis has been used as a pretext to introduce austerity measures (Grimshaw *et al.* 2012: 11). The second key trend is that, in most EU countries, public sector pay cuts and freezes have been introduced unilaterally by the state. Even in countries with a tradition of free collective bargaining in the public sector – such as Ireland, Portugal, Spain, Italy and the United Kingdom – ‘public sector employers have bypassed established collective bargaining procedures and imposed pay cuts and pay freezes unilaterally’ (Glassner 2010: 23). Third, in the majority of countries, pay adjustments have been implemented in two or three consecutive rounds. They were thus, as a rule, not introduced as a one-off emergency measure but as part of a longer and sustained strategy of putting pressure on public sector wages.

Table 2, which provides an overview of the measures implemented in those countries that were subject to direct supranational political intervention, shows that the most drastic measures have been introduced in Romania, Latvia and Greece with pay cuts of 30 per cent or more. In Romania, the wages of public sector employees were cut by 25 per cent in 2010. However, because the government also raised VAT from 19 to 24 per cent and introduced cuts in bonuses and additional payments (such as food allowances and rent subsidies), the effective wage decrease was close to 50 per cent (Glassner 2010: 19). In Greece, nominal wages were cut by an average of 14 per cent between 2009 and 2010, which together with the 17 per cent pay cut between 2011 and 2013 amounts to a total pay cut of approximately 30 per cent (Busch *et al.* 2013: 12). In Latvia,

Table 2 Public sector pay cuts and freezes in EU countries under EU, ECB and/or IMF surveillance (2008–2013)

Country	Wage cut/freeze	Unilateral state decision
Greece	Pay freeze for all earnings >€2000 per month (2009) Cuts of 12–20% in general public sector (2010) Further cut of up to 17% over three years (2011–2013)	Yes
Hungary	Pay cut of 7% (2008–2010) Abolition of 13th month salary in general public sector (2009) Pay freeze (2010–2012 or longer)	Yes
Ireland	Pay freeze for civil servants (2008–2010) General pay freeze (2010–2014) 5–7% cut in net pay as a result of pensions levy inversely related to level of income (2009) 5–8% cuts progressively related to level of income (2010)	Yes
Italy	Pay cut of 5–10% for high wage earners (2010) Pay freeze and reduced productivity bonuses (2010–2014) Suspension of automatic pay increases for certain groups of employees, such as magistrates, police force, state lawyers, military personnel and so on (2010–2013)	Yes
Latvia	Unspecified pay cuts (2008) 15–30% pay cuts (2009) Pay freeze (2010–2012)	Yes
Portugal	Pay freeze for civil servants and employees in public companies (2010–2013) 5% pay cut for higher paid civil servants (2010) 3.5–10% pay cut for salaries >€1500 per month (2011) 13th and 14th monthly pay abolished or reduced (2012–2013)	Yes
Romania	25% pay cut but cut in additional payments can mean cuts of up to 50% (2010) Abolition of a wide range of bonuses and 13th monthly pay (2011)	Yes
Spain	5% pay cut for civil servants (2010) Pay freeze for civil servants (2011–2012) 14th monthly pay abolished for all public sector employees (2012)	Yes

Source: Glassner and Keune (2012); Grimshaw *et al.* (2012); ILO (2013).

public sector wages were cut by 15 per cent in spring 2009 in return for the 7.5 billion euro loan provided by the IMF and the EU. Particularly hard hit by the cuts in public expenditure were teachers, whose wages were cut by almost one-third from September 2009 onwards (Glassner 2010: 17). These measures were particularly painful because these dramatic cuts were followed by a pay freeze between 2010 and 2012. The

pay cuts in the other countries range between 5 and 15 per cent, with wages subsequently being frozen at the lower level.

However, when assessing the real extent of the reduction in the disposable income of public sector workers, it is important to bear in mind that these figures only reflect cuts in nominal wages. Often these cuts occurred in combination with further measures, such as the abolition of thirteenth and/or fourteenth monthly wages, cuts in pension entitlements (in Greece and Spain) and other allowances, for instance for accommodation (in Portugal, Romania and Hungary), medication (in Hungary and Portugal) and food (in Portugal and Romania) (ILO 2013: 28; Vaughan-Whitehead 2012: 8).

The far-reaching cuts in the public sector in the crisis countries have also had a negative impact on the overall wage distribution. One consequence is that the public sector wage premium that traditionally exists vis-à-vis the private sector, due to the higher skills level and seniority in the public sector, has been reduced substantially. In Romania and Hungary the wage premium has even turned into a public sector wage penalty. The extreme case is Romania, where in 2009 average wages in the public sector were 45 per cent higher than in the private sector, but by the end of 2010 this wage premium had been turned upside down, with average wages in the public sector being 15 per cent lower than in the private sector (Vaughan-Whitehead 2012: 10).

4.2 Cuts and freezes of minimum wages

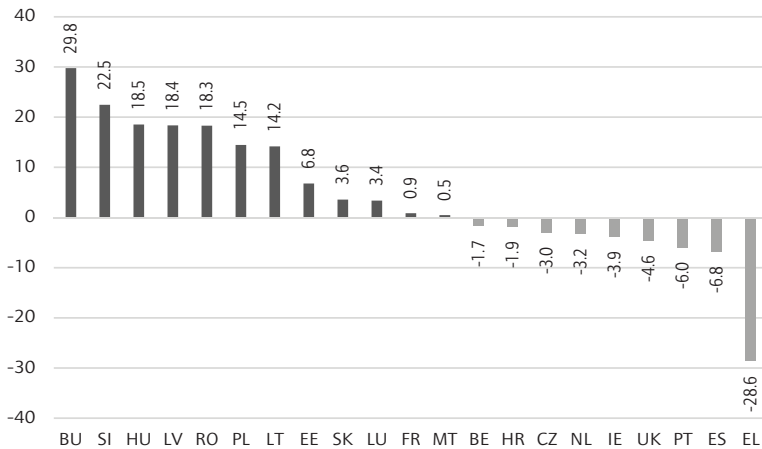
Besides public sector wages, national minimum wages offer a second opportunity for political intervention. This is all the more true for those many European countries in which the development of minimum wages not only determines the wages of those at the bottom of the wage scale, but also influences overall wage developments. This 'spillover effect' of national minimum wage developments is particularly strong in countries with comparatively weak collective bargaining systems and low bargaining coverage (for example, in many central and eastern European countries), but also in countries such as France, with relatively high minimum wage levels, where an increase in the minimum wage has an important signalling effect for overall wage developments (Aeberhardt *et al.* 2012). Moreover, national minimum wages are an obvious instrument for state intervention, as in most of the 20 out of 28 EU

member states with a national minimum wage it is statutorily determined by the state. The only exception is Belgium where the national minimum wage is set by a national collective agreement for the whole of private industry (Schulten 2014). Until recently, the same applied to Greece. However, following political pressure from the Troika (IMF 2012: 17), in November 2012 the Greek government passed a law stipulating that in future the minimum wage in Greece will be determined on a statutory basis.

Considering the impact of minimum wages on overall wage development, they also play a fairly prominent role in the new interventionist strategies at European level (for the following see Schulten 2013). The first country affected by this was Ireland, which under pressure from the Troika cut its minimum wage by 1 euro from 8.65 to 7.65 euros an hour (a decrease of nearly 12 per cent) in February 2011. After a change in the Irish government, however, the minimum wage cut was retracted and the former rate of 8.65 euros was restored in July 2011. The Troika agreed to this because the Irish government had decided to reduce social security contributions for employers in return.

In other countries – such as Latvia, Portugal and Romania, as well as, more informally, Spain – the Troika has pushed for freezes of national minimum wages. In the context of a Memorandum of Understanding, Portugal, for instance, had to agree that for the coming years minimum wage increases would be possible only with the approval of the Troika. The most radical intervention took place in Greece, where the Troika decreed a radical cut in the minimum wage of 22 per cent (and even of 32 per cent for young workers below 25 years of age), which came into effect in February 2012. Because at the time the Greek minimum wage was determined by a national collective agreement the Troika intervention was even more problematic as it openly violated the principle of free collective bargaining. After the ILO (2012a) criticised the minimum wage cut as a violation of collective bargaining autonomy and fundamental ILO Conventions, the Troika demanded that in future the minimum wage should be determined statutorily by the state. This demand was promptly implemented by the government, so that since November 2012 the Greek minimum wage has been determined on a statutory basis.

The political pressure put on minimum wages during the past four years (2010–2013) led to a drop in the real value of the minimum wage – that is, the nominal value of minimum wages deflated by consumer prices

Figure 1 Development of real national minimum wages, 2010–2013 (%)*

Note: *Increase or decrease from 1 January 2010 to 1 January 2014, deflator of consumer prices

Source: WSI Minimum Wage Database 2014

– in nine out of 21 EU member states (Figure 1). The decrease was particularly strong in countries under the surveillance of the Troika (Greece, Portugal, Spain and Ireland) as well as in the United Kingdom, the Netherlands and the Czech Republic. On the other hand, in a few eastern European countries the real minimum wage value has shown remarkably high growth rates. This includes Hungary, where the unusually high increase in the minimum wage served mainly to compensate for the effects of a new flat-rate tax reform, which led to a significant tax increase for low wage earners (Szabó 2013).

A rise in the minimum wage with the intention of raising the minimum wage level above the poverty line also occurred in Slovenia in 2010. Meanwhile, the comparatively high minimum wage level in Slovenia was criticised by DG ECFIN (Stoviček 2013). The same applies to the relatively high minimum wage level in France. With regard to both countries, DG ECFIN alleged that the development of minimum wages negatively influences price competitiveness. ‘Moderate development’ of the minimum wage was therefore one of the main emphases of the country-specific recommendations issued for both countries in the context of the European Semester in 2013 and 2014.

4.3 Decentralisation and dismantling of multi-employer collective bargaining

Apart from direct intervention in wage developments through cuts and freezes of public sector and minimum wages, in many European countries the most fundamental changes have concerned the wage-setting and collective bargaining institutions (for an overview see Marginson and Welz 2014; Waas 2013). Although the current economic crisis has reinforced the decentralisation of collective bargaining throughout Europe, this process has been most pronounced in countries subject to direct supranational intervention by the Troika (Schulten and Müller 2014a). In exchange for financial assistance, the Troika has asked in all countries for ‘structural reforms’ which always also include more or less far-reaching changes to national collective bargaining systems. Irrespective of specific national traditions and structures of industrial relations, the Troika has pursued the same strategy of a radical decentralisation of collective bargaining in all cases.

In the meantime, all the ‘Troika’ countries have introduced more or less far-reaching changes to their collective bargaining systems (see Table 3).⁴ Concerning the changes that have been made, three groups of countries can be distinguished. The first group comprises Ireland and Romania, which before the reforms were characterised by a comparatively high level of bargaining centralisation, involving national cross-sectoral agreements that defined the terms of reference for lower-level negotiations (Visser 2011: 41). In these two countries, the austerity-driven changes led to an almost complete breakdown of multi-employer bargaining. In Ireland this was the result of the employer federation IBEC’s withdrawal from the national agreement following the failure of talks on the implementation of the wage agreement concluded in 2008, which after 22 years of cross-sectoral wage determination brought the return of company-level bargaining (Doherty 2011). In Romania, cross-sectoral bargaining was essentially abolished by the government’s unilateral introduction of the Social Dialogue Act in 2011 (Trif 2013). Further pressures towards decentralisation resulted from the government’s tightening the rules on the extension and application of sectoral agreements and increasing the threshold for the representativeness of trade unions as a precondition to negotiate agreements.

4. For a detailed list of measures and legal changes in the various countries see Appendix 1.

Table 3 Decentralisation of collective bargaining system in EU countries under EU, ECB and/or IMF surveillance

Measures	Affected countries
Abolition/termination of national collective agreements	Ireland, Romania
Facilitating derogation of firm-level agreements from sectoral agreements or legislative (minimum) provisions	Greece, Portugal, Hungary, Italy, Spain
General priority of company agreements/abolition of the favourability principle	Greece, Spain
More restrictive criteria for extension of collective agreements	Greece, Portugal, Romania
Reduction of the 'after-effect' of expired collective agreements	Greece, Spain
Possibilities to conclude company agreements by non-union group of employees	Greece, Hungary, Portugal, Romania, Spain

Source: Authors' compilation based on Appendix 1.

The second group of countries consists of Greece, Italy, Portugal and Spain, which represent the 'Mediterranean model' of labour relations, marked by a long tradition of well-established sectoral bargaining structures (Meardi 2014). All Mediterranean countries have enjoyed comparatively high levels of collective bargaining coverage of 80 to 90 per cent, which was backed by direct – or in the case of Italy, indirect – *erga omnes* regulations and extensions of collective agreements (Schulten 2012b). Although the multi-employer bargaining structures remained formally intact, their scope and actual operation was increasingly undermined by the various legal changes that have been introduced in response to the demands placed upon these countries by the Troika. The most radical decentralisation took place in Greece (Dedoussopoulos *et al.* 2013; Patra 2012) and Spain (Molina and Miguélez 2013; Nieto 2012). Both countries gave company agreements a general priority over sectoral agreements, and abolished the 'favourability principle', which has allowed company agreements to undermine sectoral standards. In the case of Italy (Pedersini 2013) and Portugal (Campos Lima 2013; Palma Ramalho 2013), the decentralisation of collective bargaining is still promoted in a more organised form, as the possibilities for downward derogation from sectoral standards at company level remain dependent on the commitment of the bargaining parties at sectoral level. However, in Italy the

legal reforms of September 2011 increased the scope for companies to derogate not only from collective agreements but also from legislative minimum provisions. The case of Fiat, furthermore, has shown that companies are able to withdraw from the sectoral bargaining system and to set up their own company agreement (Tomassetti 2013). In Portugal, the bargaining system has been further weakened by the introduction of more restrictive criteria for the extension of collective agreements. Before the reform, all major collective agreements were declared generally binding in a quasi-automatic way. Finally, Greece, Portugal and Spain have made it easier for non-union employee representatives to conclude collective agreements, in particular in small and non-unionised companies, which has further weakened the position of trade unions.

The third group of countries affected by changes in national collective bargaining systems that have been promoted by the IMF, in cooperation with the other Troika institutions, comprises Hungary and Latvia. Both countries have – as is the case in the majority of CEE countries – a fairly fragmented, company-level single-employer bargaining system with a comparatively low level of collective bargaining coverage. Thus, there was not much scope for further decentralisation. In Latvia, attempts by the social partners to establish sectoral collective bargaining structures were abandoned in the context of the crisis (Karnite 2013). While in Latvia the brunt of austerity measures has been borne by the public sector in the form of extensive wage cuts (Kallaste and Woolfson 2013), the legal changes introduced in Hungary in 2011 were aimed primarily at weakening the bargaining power of trade unions, for instance by curtailing the right to strike in public services, abolishing the only tripartite national forum for discussing recommendations on minimum wage increases and allowing works councils to negotiate company-level agreements if there is no trade union present at the workplace (Szabó 2013).

The fundamental changes in the collective bargaining systems of the European ‘programme countries’ were promoted in more or less close cooperation between national and European actors. In most cases, however, the Troika was the driving force behind these far-reaching reforms. At the same time, the Troika was used by national governments to legitimise the introduction of measures that have been demanded by certain national actors for a long time. Especially with regard to the neoliberal transformation of national collective bargaining systems the new European interventionism played a crucial role. What European market integration left unfinished is now being driven forward by the Troika: the convergence

of national collective bargaining arrangements towards a highly decentralised system of the kind that already exists in the United Kingdom and in many central and eastern European countries (Meardi 2014).

However, such a system change implies not only a decentralisation but also a de-collectivisation of labour relations, because collective bargaining coverage is usually much higher in countries with strong multi-employer bargaining than it is in countries with mainly company-level bargaining. The data presented in Table 4 illustrate the dramatic decline of collective bargaining coverage in some of the ‘programme countries’ as a result of the far-reaching changes that have been introduced during the crisis. In Spain, for instance, the number of branch-level collective agreements was essentially halved between 2008 and 2013 from 1,448

Table 4 Collective agreements and bargaining coverage in Greece, Portugal and Spain, 2008–2013*

	2008	2009	2010	2011	2012	2013
Greece						
Branch-level agreements	202	103	91	55	31	14
Company-level agreements	462	347	352	241	978	408
Portugal						
Branch-level agreements	172	142	141	93	36	27
Company-level agreements	124	110	89	78	66	68
Total agreements	296	252	230	171	102	95
Number of extension decrees	131	101	116	17	12	9
Workers covered by collective agreements (million)	1.7	1.3	1.4	1.2	0.3	0.2
Spain						
Branch-level agreements	1,448	1,366	1,265	1,163	1,113	706
Company-level agreements	4,539	4,323	3,802	3,422	2,893	1,702
Total agreements	5,987	5,689	5,067	4,585	4,006	2,408
Workers covered by collective agreements (million)	12.0	11.6	10.8	10.7	9.9	7.0

Note: * newly concluded collective agreements in the respective year.

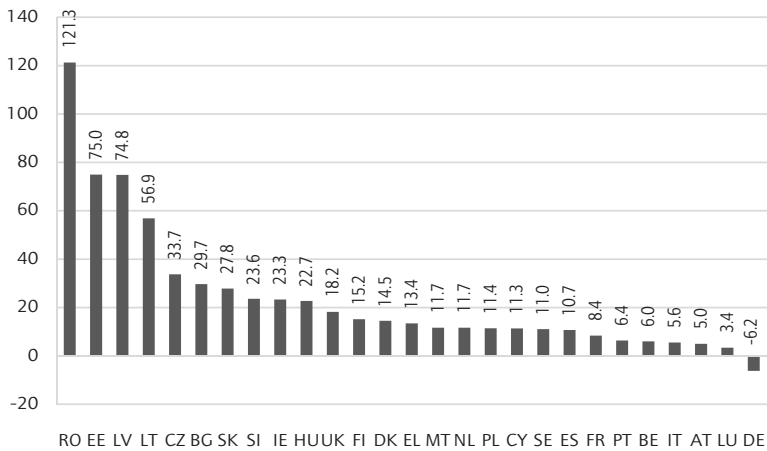
Sources: Ministry of Labour in Greece, Portugal and Spain.

to 706. Company-level agreements declined even more, by roughly two-thirds. As a consequence, the number of workers covered by collective agreements decreased from 12 million in 2008 to just 7 million in 2013. In Portugal the decline in collective bargaining coverage was even more dramatic. There, the total number of registered collective agreements dropped from 296 in 2008 to 95 in 2013. Because, at the same time, the number of extended collective agreements fell from 131 in 2008 to only 9 in 2013, the number of workers covered by collective agreements virtually collapsed, from 1.7 million in 2008 to 200,000 in 2013. In Greece, the number of newly-concluded sectoral collective agreements decreased from 202 in 2008 to only 14 in 2013. The strong increase in company-level agreements in 2012 can be explained mainly by the fact that many companies used the new rules introduced in October 2011 to negotiate company-level wages which remained below the existing sectoral wage level (Daouli *et al.* 2013).

4.4 Changing pattern of European wage developments

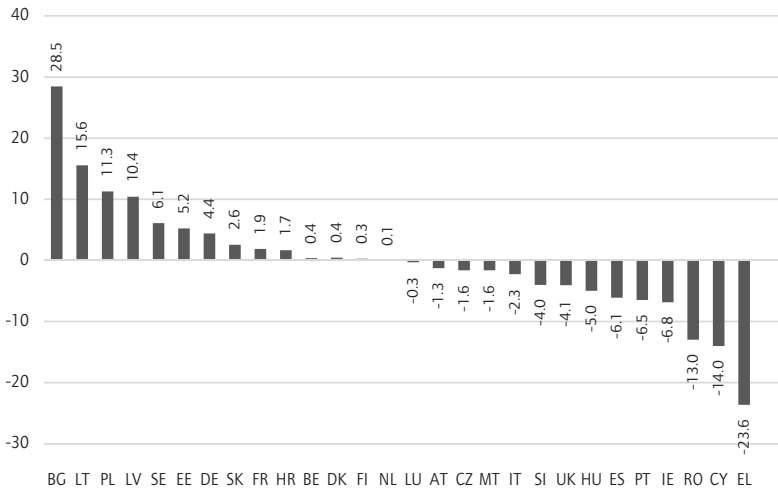
Against the background of widespread wage freezes and cuts, as well as a comprehensive reconstruction of collective bargaining in many European countries, the implications of the new European interventionism are manifest in the fundamentally changed pattern of wage developments in Europe (see Figures 2 and 3; see also OECD 2014). In the decade up to 2009, almost all EU member states registered positive real wage developments. The strongest increases took place in some central and eastern European countries, followed by substantial wage growth in countries such as Ireland or Greece, and more moderate increases in countries such as Italy, Spain and Portugal. The sole exception was Germany, the only country during that period with a strong decrease in real wages.

Since 2010 the picture has virtually reversed. Only a few countries have registered – mainly modest – real wage increases, while in 14 of the 28 EU countries real wages have fallen. By far the biggest cut has been in Greece, with a fall of more than 23 per cent, followed by Cyprus with 14 per cent, Romania with 13 per cent and the rest of the ‘Troika countries’, namely Ireland (–6.8 per cent), Portugal (–6.5 per cent) and Spain with a fall of 6.1 per cent. While the Troika welcomes this development as a necessary ‘adjustment process’ (for example, European Commission 2012d), from a more critical perspective it looks more like a strong European-wide downward wage spiral, which obviously depresses consumer

Figure 2 Development of real wages, 2001–2009 (%)*

* Nominal compensation deflated by the national HCPI

Source: AMECO Database, calculations by the WSI

Figure 3 Development of real wages, 2010–2014 (%)*

Note: * Nominal compensation deflated by the national HCPI. Figures for 2014: Forecast by the European Commission (Spring 2014)

Source: AMECO Database, calculations by the WSI

demand, fosters deflationary tendencies and therewith contributes to consolidating economic stagnation in Europe.

5. Outlook: What future for a European wage policy?

The new system of European economic governance has led to a new European interventionism in the area of wage policy; this marks a paradigm shift from the acceptance of free collective bargaining to direct political intervention in national collective bargaining outcomes and processes. The key objective of this new European interventionism is to use wages as the central adjustment variable in order to close the (cost-)competitiveness gap between ‘surplus’ and ‘deficit’ countries in Europe. By now, it is abundantly clear that the EU crisis management based on the combination of austerity policies and neoliberal structural reforms has not only been ineffective in addressing the problem of macroeconomic imbalances, but has even aggravated the debt and growth problems of deficit countries (Holland 2012). Even the IMF has stated that the austerity policies might have gone too far, because they are obviously depressing economic growth and are contributing to sharp increases in unemployment (Blanchard and Leigh 2013). However, this has not stopped the IMF from continuing to support intervention in national collective bargaining processes (Blanchard *et al.* 2013).

The interventionist approach of cutting wages is questionable in at least two respects. First, it views wages primarily as a cost factor and neglects the important role of wages in creating or stabilising domestic demand. Thus, particularly in the European deficit countries, in which growth relies more heavily on domestic demand than on exports, the potential positive effects of falling wages and unit labour costs on net exports is more than offset by the negative impact of falling wages on domestic demand. The promotion of an export-oriented growth model as a way out of the crisis overstates the importance of the export sector for overall economic growth (Feigl and Zuckerstätter 2012).

Secondly, the narrow focus on cost competitiveness ignores the fact that the primary reason for the increasing macroeconomic imbalances is not wage developments but the different economic structures of the various countries (Felipe and Kumar 2011). Wage cuts therefore help to reduce current account deficits only in that they deplete domestic demand, which in turn reduces imports. Wage cuts, however, do little to improve

the competitiveness of the Mediterranean countries vis-à-vis the northern European surplus countries. This is because the deficit countries either lack the industrial structures needed to pursue an export-oriented growth strategy or their industrial structures are so different from those in the northern European countries that they are in direct competition with countries from outside the EU rather than with the northern European surplus countries.

However, maybe even more problematic than the economic effects of the current wage policy in Europe are the long-term and structural consequences of the new European interventionism. These manifest themselves in the neoliberal transformation of national collective bargaining systems aimed at radically decentralising and dismantling multi-employer bargaining arrangements. This applies in particular to the countries under the surveillance of the Troika.

As a result, there has been convergence of collective bargaining structures within the group of 'crisis countries', with the Mediterranean countries moving closer towards the fragmented and decentralised model of collective bargaining that is characteristic of the majority of CEE countries (Meardi 2014). At the same time, the new European interventionism has increased the divergence between the 'crisis countries' and the so-called 'core countries' of the EU (comprising Austria, the Benelux countries, France, Germany and the Nordic states), where collective bargaining institutions remained fairly stable and where the crisis – if at all – reinforced the already existing trend of controlled decentralisation, without, however, substantially undermining the dominant role of sectoral-level bargaining (Schulten and Müller 2014a). However, the fact that so far only the Mediterranean countries are affected by this convergence trend does not mean that the 'core countries' are immune to the new European interventionism and the resulting political pressure to decentralise their collective bargaining systems. In the country-specific recommendations, Belgium, for instance, was repeatedly requested to decentralise its bargaining system by 'facilitating the use of opt-out clauses from sectoral collective agreements to better align wage growth and labour productivity developments at local level' (European Council 2012: 14). Another country under strong pressure to reform its wage-setting system is France. Accordingly, the national agreement on a 'new economic and social model', which was concluded in January 2013, makes it easier for companies to sign company-level agreement which temporarily derogate from the norms of the collective agreement in return for a commit-

ment to secure employment (Turlan and Cette 2013). Moreover, if the currently proposed system of European competitiveness pacts becomes reality, the experiences made in the ‘neoliberal laboratory of Southern Europe’ might spread across the whole EU (Oberndorfer 2013b).

The overall objective of the new European interventionism is to force EU member states to overcome all the ‘rigidities’ that hamper the downward flexibility of wages, including trade union bargaining power. Beyond that, European interventionism has a strong political dimension. DG ECFIN could not have been clearer in its report on labour market developments in 2012, in which it classifies ‘the overall reduction in the wage-setting power of trade unions’ (European Commission 2012d: 104) as a desirable outcome of labour market reforms. Against this background, it is becoming increasingly clear that the new European interventionism must also be seen as a political project to weaken European trade unions.

Against the background of increased mass unemployment in many European countries, it is, of course, fairly difficult for trade unions to counter such a strategy. However, there are at least three core elements that mark an alternative approach towards a European wage policy. First of all, European trade unions (but also employers⁵) need to defend the principle of collective bargaining autonomy against the increasing state interventionism at European and national level (Janssen 2013). One way to do this is to use judicial channels by filing formal legal complaints against political intervention in free collective bargaining at national constitutional courts, as well as at international organisations such as the Council of Europe and the ILO (Clauwaert and Schoemann 2013; Fischer-Lescano 2014). In the case of Greece, for instance, the ILO confirmed that the Troika-imposed intervention in national collective bargaining practices violates ILO Conventions No. 87 and No. 98 (ILO 2012a). Even though the ILO cannot force national governments to change legislation, the ILO’s verdict lends important moral and political support to the trade unions’ position so that the European policymakers cannot continue to ignore the strong political signals coming from international and European institutions (ETUI 2014).

5. The fact that the defence of free collective bargaining is not only a trade union issue is demonstrated by a statement by the Council of European Employers of the Metal, Engineering and Technology-Based Industries which ‘insists ... that the EU institutions must respect the autonomy of social partners/employers and workers and do not intervene with wage setting at any level’ (CEEMET 2012).

A further central element of a trade union counter-strategy is to strengthen the unions' own attempts towards a European coordination of collective bargaining. The traditional trade union wage coordination rule, according to which real wages should at least increase in line with productivity growth (Schulten 2002), is still very important as a bottom line to prevent downward wage competition. Moreover, a more proactive approach might turn the currently dominating European wage policy on its head by strengthening multi-employer collective bargaining institutions in order to support a more sustainable wage-led growth regime in Europe (Stockhammer and Onaran 2012). A first step in this direction could be the development of a 'European minimum wage policy' in order to make sure that every worker in Europe receives a wage that ensures a decent standard of living (Schulten 2012a; Schulten and Müller 2014b).

Such an alternative approach towards a European wage policy has been supported by, for example, the ILO, which in its 'Global Wage Report' emphasises that in order to avoid an austerity-induced recession, it is important to stimulate domestic demand by, among other things, strengthening wage-setting institutions (ILO 2012b: 62/63). There is also some support for this within the European Commission, as at least DG Employment has taken a much more nuanced approach than their colleagues from DG ECFIN by explicitly acknowledging the function of wages in generating domestic demand and strengthening social inclusion (European Commission 2012e, 2012f). In light of meagre price development there even seems to be a growing awareness that a continuation of wage freezes and cuts will further increase the danger of a European-wide deflation crisis (for example, OECD 2014).

Therefore, there is a strong need to overcome the currently dominant narrative of European policymakers and national governments, according to which wages are seen as the core adjustment variable to economic imbalances in Europe. Instead of the narrow focus on wages, there should be a much broader approach to alternative macroeconomic policy coordination in Europe, whereby European wage coordination would primarily have the function of avoiding deflationary tendencies triggered by downward wage competition and contributing to a more sustainable, demand-led economic development model (EuroMemoGroup 2013; Hein *et al.* 2005; Hein *et al.* 2011).

Appendix 1 Major changes in collective bargaining systems in EU countries under EU, ECB and/or IMF surveillance

Greece	<p>Law No. 3899/2010 of 17 December 2010: Introduction of new type of a 'special company-related collective agreement' in companies in significant financial straits: these new company agreements may provide for wages and other working conditions that are less favourable than those provided for by the respective sectoral collective agreement, but not less favourable than the minimum conditions agreed in the national collective agreement. The new company agreements could be signed either by the unions at company level, or – where they do not exist – by the sectoral union organisations.</p> <p>Introduction of stricter criteria for extension of sectoral agreements: extension is allowed only when the employers under the agreement represent at least 51 per cent of the workforce in the respective sector.</p> <p>Law No. 4024/2011 of 27 October 2011: Introduction of a general priority for company agreements over sectoral agreements and a general abolition of the favourability principle. In companies without trade unions or with less than 50 employees, company agreements can also be concluded by 'other associations of employees' which represent at least 3/5 of the workforce.</p> <p>Law No. 4046/2012 of 14 February 2012: Reduction of the after-effect of expired collective agreements to three months.</p> <p>Law No. 4093/2012 of 07 November 2012: The national minimum wage is no longer determined by a national collective agreement but instead statutorily by the state.</p>
Hungary	<p>Revision of Labour Code of 26 October 2011: Introduction of the right to conclude collective agreements for works councils, provided that there is no trade union at company level whose membership covers at least 10 per cent of the employees. The revised Labour Code furthermore allows collective agreements and individual work contracts to regulate working conditions differently to what is stipulated in the law – this includes the possibility of agreements derogating from the law to the benefit of the employer.</p>
Ireland	<p>December 2009: Breakdown of the 22 year-old centralised pay bargaining system after the employers withdrew from the national social partnership agreement.</p> <p>Industrial Relations (Amendment) Act 2012: More restricted regulation on the so-called 'Registered Employment Agreements' (REAs), as well as on 'Employment Regulation Orders' (EROs), which determined certain minimum wages and conditions in a limited number of sectors (for example, agriculture and construction). Companies now have the option to diverge from these conditions.</p>
Italy	<p>National collective agreement of 22 January 2009: Introduction of a general opening clause for wage regulations deviating from sectoral agreements at company level (the agreement was not signed by the largest Italian trade union federation CGIL).</p> <p>National collective agreement of 28 June 2011: All sectoral agreements shall contain opening clauses, according to which there may be deviation at the enterprise level from sectoral standards under certain circumstances (economic difficulties, restructuring, introduction of significant new investment). Such deviations must be agreed in an enterprise collective agreement signed by the majority of the Rappresentanze Sindacali Unitarie (RSU) (unitary workplace union structures). The workforce must confirm the deviating company agreement if one of the signatory trade unions or at least 30 per cent of the employees request it.</p>

Appendix 1 Major changes in collective bargaining systems in EU countries under EU, ECB and/or IMF surveillance (cont.)

Italy (cont.)	Law No. 148 of 14 September 2011: Company collective agreements can deviate downwards from sectoral agreements and certain labour law provisions. Possibilities to deviate from collective agreements at enterprise level concern almost all aspects of labour and employment conditions (including wages and wage structures, working time, atypical employment and employment protection). The company agreement must be signed by a majority of the representative trade unions in the enterprise.
Portugal	Law No. 23/2012 of 25 June 2012 (approved Draft Law No. 46/XII of 2 February 2012): In companies with 150 or more employees, collective agreements can be concluded by works councils, if the trade unions have authorised them to do so. Council of Ministers' Resolution No. 90/2012 of 10 October 2012: Introduction of stricter criteria for the general extension of collective agreements, according to which an employer covered by ten agreements has to represent at least 50 per cent of the employees of certain sector.
Romania	Law No. 62/2011 of 10 May 2011: – Abolition of the national collective agreement – Abolition of the automatic extension (<i>erga omnes</i>) of sectoral agreements; extension is possible only if more than 50 per cent of all employees in the sector work for companies that are members of the signatory employers' organisations. – A trade union can negotiate company agreements only if it organises more than 50 per cent of the workforce in the company. – If there is no union in the company, agreements can be concluded with other employee representatives
Spain	Royal Decree 10/2010: Improved options for making use of hardship clauses at company level which allow temporary deviation from sectoral agreements. If agreement cannot be reached, an arbitration board can be called in. Royal Decree 7/2011 of 10 June 2011: Extension of possibilities to use opening clauses at company level to derogate from sectoral agreements. Law 3/2012 of 6 July 2012 (approving Royal Decree 3/2012 of 10 February 2012): – Introduction of a general priority of company agreements over sectoral agreements. – Possibility to deviate from sectoral collective agreements by means of company agreements. Company-level options for such deviations concern almost all aspects of employment and working conditions (including wages and wage structures, working time, social benefits). – In companies without union representation, company agreements can be concluded by non-union groups of workers. – Limitation of the after-effect of expired collective agreements to one year (previously unlimited).

Source: Authors' compilation on the basis of Busch *et al.* (2013); Clauwaert and Schömann (2012); European Labour Law Network (<http://www.labourlawnetwork.eu/>)

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EU country codes

AT	Austria
BE	Belgium
BG	Bulgaria
CY	Cyprus
CZ	Czech Republic
DE	Germany
DK	Denmark
EE	Estonia
EL	Greece
ES	Spain
FI	Finland
FR	France
HU	Hungary
IE	Ireland
IT	Italy
LT	Lithuania
LU	Luxemburg
LV	Latvia
MT	Malta
NL	Netherlands
PL	Poland
PT	Portugal
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SE	Sweden
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SK	Slovakia
UK	United Kingdom