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## **PART III: A DYNAMIC LABOUR FORCE**

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**Summary**

- The EU has as many industrial relations models as it has Member States. Both trade unions and employers' associations are organised in very different ways in different countries. Wage bargaining, whatever its framework, should support employment.
- Collective bargaining may occur primarily at a company, sector or cross-sector level, and may be coordinated to a greater or lesser extent, reflecting national traditions, practices, institutions and cultures. The degree of coordination has implications for the way in which labour market policy is delivered.
- Governments are also employers. The size of the public sector payroll has implications for a government's ability to directly influence wage growth; for the location and distribution of employment; for social dialogue; and for the fiscal implications of wage growth, retirement patterns and demographics.
- Cross-border coordination of collective bargaining has been pursued by some social partners and has, in some cases, resulted in a broader exchange of information and understanding between the organisations concerned. Wage bargaining, however, retains its distinctively national characteristics.

**Fifteen EU models, not one 'EU Model'**

**8.1** Wage bargaining must support employment. There is, however, no one model of bargaining. Industrial relations – the regulation of work and employment – encompasses a multiplicity and variety of processes, actors, institutions, and economic and social frameworks. To describe just a few of the differences between national systems:

- accepted rights and obligations on the part of employees and employers differ between Member States, as does the extent to which these rights and obligations become institutionalised. For example, some systems give explicit legal protection of status as well as contract; others have a tradition of voluntarism, and only a very limited explicit statutory definition of employee rights;
- some are characterised by a high degree of coordination between and among social partners; some are centralised; others are decentralised and/or uncoordinated;
- some recognise a wide range of stakeholder interests, preferably aligned by organised collective representation, with legitimate influence over corporate decision-making; others judge it wiser to focus primarily on shareholders.
- in some systems, trade unions and/or employer bodies are involved in the administration of parts of the welfare system, or the formation of economic policy. In others, the role of the social partners is, outside the workplace, confined to commentary; and
- some systems lean towards substantive and encompassing regulation, setting at least basic standards for many aspects of the employment relationship; others give priority to procedural regulation, defining the processes of interaction by which substantial rules are constructed.<sup>1</sup>

<sup>1</sup> Discussed further in *The Europeanisation – or the Erosion – of Industrial Relations?* R. Hyman, *Industrial Relations Journal*, 32:4, September 2001.

**8.2** In each of these examples the UK tends to be put into the latter group. However, in reality matters are not always so clear cut. The UK has, for example, a tradition of voluntarism and, over the past thirty years, an explicit statutory definition of employee rights; the former generally refers to collective rights, the latter to minimum standards for individual rights.

**8.3** Furthermore, tempting as it is to portray a UK or Anglo-Saxon ‘model’ standing next to and contrasting with a European or Rhineland ‘model’, the rest of the EU does not comprise one collective alternative. The UK ‘model’ is one not of two but of several models, all of which are evolving to meet the needs of a changing workforce in a changing Europe.

**8.4** This and the next chapter take a closer look at industrial relations across the EU, beginning here with collective bargaining, in particular examining the labour market institutions, the bargaining frameworks, the extent of cross-border coordination in wage bargaining and, of course, the outcomes.

**New challenges in a changing Europe**

**8.5** While the EU has as many industrial relations models as it has members, most sprang initially from the need to meet (or counter) the demands of a full-time, predominantly male and primarily manufacturing industrial base. As such, all are now in the process of adapting to a different type of workforce with different demands, expectations and abilities, and in a very different Europe.

**Trade unions**

**8.6** Trade unions play an important role in protecting individuals against unfair abuses of power at the workplace, in ensuring fair treatment and in providing an effective voice for employee and, in many cases, pensioner interests. Some trade unions have a substantial proportion of retired members. Around a fifth of the large French CGT union, for example, are pensioners.

**8.7** The most common structure of trade union organisation is one of sector-based unions grouped in a number of confederations. As Table 8.1 shows, however, this is far from being a representative European model.

**Table 8.1: Trade union organisational structures**

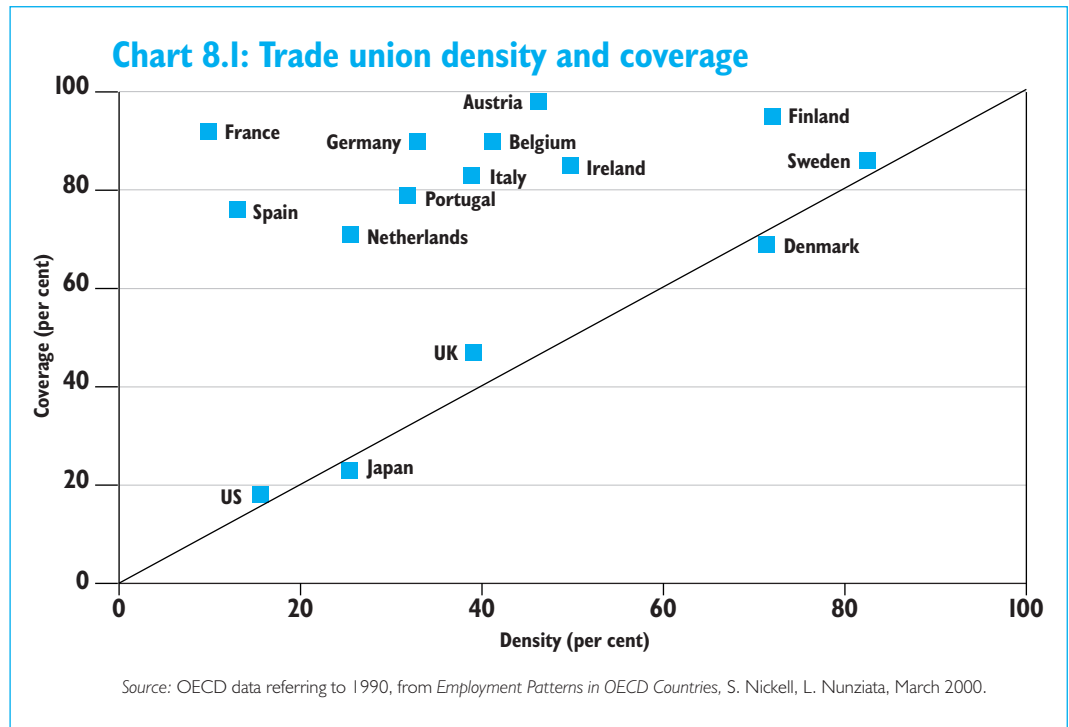
	<b>Structured primarily around industries/sectors</b>	<b>Mixed structures – industry, general, occupational</b>
Single main confederation	Austria, Germany	Ireland, UK, US
Multiple confederations (often along religious, political or organisational lines)	Belgium, France, Italy, Japan, Luxembourg, Netherlands, Portugal, Spain	Denmark, Finland, Greece, Norway, Sweden

*Source: European Industrial Relations Observatory*

**8.8** Trade union density, (the proportion of wage or salary earners who are members of a trade union) has in general declined as working patterns have changed, as manufacturing’s share of employment has fallen, as the share of women in the labour force has increased, and as changes in legislation have affected the relative ease and appeal of union membership.

**8.9** Union membership is not, however, necessarily an accurate reflection of the economic importance of trade union collective bargaining. In many countries, increases in pay and terms agreed by unions and employers are extended across the relevant sector by law or convention. Trade Union coverage (the percentage of wage or salary earners covered by a collective agreement) is in most EU countries considerably greater than trade union density, as Chart 8.1 illustrates. (more recent 1999 figures for the UK suggest trade union density of around 30 per cent, and coverage of around 36 per cent.<sup>2</sup>)

<sup>2</sup>Has UK Labour Market Performance Changed? S. Nickell, speech to Society of Business Economists, May 2001.



**Employers' associations** **8.10** Employers may be organised on either a sector or inter-sector basis and, in most EU countries, pursue collective bargaining or substantive dialogue with trade unions through their employer associations (Table 8.2). The UK differs from other EU countries (but resembles the US) in that its own employer organisations do not play a significant bargaining role at either a sector or cross-sector level.

**Table 8.2: Bargaining role of employers' organisations**

	<b>Bargaining or significant dialogue with unions</b>	<b>Little/no bargaining or dialogue with unions</b>
Cross-sector organisations	Austria, Belgium, Denmark, Finland, France, Germany, Greece, Ireland, Italy, Japan, Luxembourg, Netherlands, Portugal, Spain, Sweden	UK, US
Sector organisations	Austria, Belgium, Denmark, Finland, France, Germany, Greece, Italy, Netherlands, Portugal, Spain, Sweden	Ireland, Japan, Luxembourg, UK, US

Source: *European Industrial Relations Observatory*

**Different levels of wage bargaining in different Member States...** **8.11** Wage bargaining occurs in different countries at different levels, as Table 8.3 illustrates.

**Table 8.3: Wage bargaining levels**

	Intersectoral level	Sectoral level	Company level
Austria		XXX	X
Belgium	XXX	X	X
Denmark	XX	XX	X
Finland	XX	XX	X
France		X	XXX
Germany		XXX	X
Greece	X	XXX	X
Ireland	XXX	X	X
Italy		XXX	X
Luxembourg		XX	XX
Netherlands		XXX	X
Portugal		XXX	X
Spain		XXX	X
Sweden		XXX	X
UK		X	XXX

X =evident XX=important XXX=dominant

Source: European Industrial Relations Observatory

**8.12** In most Member States, wage bargaining occurs primarily at the level of the industry or sector. In Belgium (Box 8.1) and Ireland (Box 8.2), however, cross-sector agreement at a national level sets the pace and the ceiling. In Finland, the dominant level of bargaining varies between the cross-sector and sector levels; in the UK and France, company-level bargaining is the norm.

**8.13** The frameworks described in Table 8.5 are not set in stone. In the UK, the primary level of wage bargaining shifted during the 1980s from the sector to the company.<sup>3</sup> In Italy, the wide-ranging tripartite accord of July 1993 replaced previously multi-level bargaining with sector agreements running for four years (two years for pay), supplemented by company level bargaining on matters not covered at a national level.

**8.14** French sector bargaining, already fragmented, became even more so during the 1990s, while pay bargaining in the Netherlands became less centralised in some sectors (e.g. banking), more so in others (e.g. catering). Sweden has moved from inter-sector to sector level deals; Spain, from the company level to the sector.

<sup>3</sup> *All change at work? British Employment Relations 1980–98*, N. Millward, A. Bryson, J. Forth, Routledge, 2000

**Box 8.1: Belgium; aiming to preserve its competitiveness**

Belgium's **Central Economic Council** was set up in 1948 and includes employer, trade unions and independent representatives. Following the 1989 Preservation of the Country's Competitiveness Act, the Council is required to report twice a year on the competitiveness of Belgian companies. Its reports form the basis of negotiations between the government and social partners and – if necessary – of any government measures to restore or preserve competitiveness.

In 1996, and after a sustained loss of competitiveness and several wage freezes, legislation was enacted to constrain wage increases and align them with estimated pay trends in France, Germany and the Netherlands. Every year, the Council prepares a technical report on the maximum permitted rise in nominal labour costs, given expected pay trends in these three trading partners.

Every second year, and within the framework of a national, cross-sector agreement, the social partners then set the maximum permitted increase in labour costs. This margin constrains pay scales, wage indexation payments and other negotiated benefits. If they cannot agree a figure, the government imposes one (and may also step in if it believes the agreed margin is incorrect, as in 1996). Cross-sector agreement to a pay norm then paves the way for subsequent sector negotiations.

For 2001-2002, the indicative hourly pay norm is 6.4 per cent. In high performing sectors this may rise to (but not exceed) 7 per cent. The cross-sector agreement also makes provisions on holiday pay, training, work time, employers' social security contributions, older workers, and harmonisation of blue and white collar status.

**8.15** Exactly what cross-sector or sector pay bargaining entails, varies between countries and sectors. Sector wage deals, for example, may be national, or they may apply only within a particular region (as in Germany). They may involve primarily small and medium sized enterprises, with larger firms bargaining on an individual basis. A sector or cross-sector deal may determine a minimum increase in pay which is added to in company-level bargaining (Denmark); alternatively, cross-sector agreement on a maximum wage increase may set an upper limit for negotiations at a sector or company level (Belgium, Ireland).

**8.16** A stable pay bargaining structure over time does not, however, imply that the flexibility afforded to companies within this structure remains unchanged. A shift in bargaining from the sector to the company level may enhance companies' freedom for manoeuvre. So too, however, may a shift in sector bargaining practice from agreeing specific pay rises, to agreeing bands for pay rises; so, too, may an agreement which allows companies to pay less than an industry-agreed pay increase if circumstances dictate (or more, if circumstances permit).

**Box 8.2: Ireland's Programme for Prosperity and Fairness**

The current tripartite national agreement, the Programme for Prosperity and Fairness (PPF), was formally endorsed in March 2000. The fifth such agreement in succession since 1987, it expires at the end of 2002.

The PPF originally provided for pay increases of at least 15 per cent over 33 months, as well as a range of measures on tax, equality, transport, housing, rural development and social inclusion. In the face of rising inflation and employee pressure, however, the pay range was revised up by 3 per cent only nine months after the PPF's endorsement. Employers gained some concessions in return; in particular, a reinforced industrial peace clause monitored by a new National Implementation Body, and extension of the 'inability to pay clause' for firms exposed to difficult competitive conditions. The Government cut direct and indirect tax rates in its 2001 budget.

**8.17** Such developments also allow account to be taken of regional productivity differences within sector-level agreements. Most industry-wide pay demands are based on a combination of inflation and national (or sector) productivity growth. Regional differences in productivity are – whether because of solidarity, equity or simply complexity – rarely taken into account. Incorporating pay ranges or opt-outs into sector agreements can, however, allow some adjustment to regional differences, without adopting a decentralised system. There is more to flexibility than the level of wage bargaining.

...and different  
degrees of  
coordination  
between wage  
bargainers

**8.18** Decentralised bargaining does not imply uncoordinated bargaining. Japan, for example, has one of the most decentralised bargaining systems in the world, but is far from uncoordinated; Germany's system of regional sector bargaining is not centralised, but highly coordinated.

**8.19** Table 8.4 examines degrees of coordination, ranging from national or cross-sector pay agreements, e.g. Ireland, to coordinated guidelines between union and employer bodies, e.g. Netherlands, to situations in which one industry or region sets a benchmark for others to follow, e.g. Germany.

**Table 8.4: Wage bargaining coordination within countries**

	National or cross-sector agreement	Coordination between union or employer bodies	One sector leads; others follow	Pay indexation	Statutory minimum wage
Austria			XX		
Belgium	XX			XX	X
Denmark	X	X	XX		
Finland	XX	X	X		
France					X
Germany	X	X	XX		
Greece	XX				X
Ireland	XX	X			X
Italy	XX				
Luxembourg				XX	X
Netherlands	X	XX	X		X
Portugal	XX				X
Spain		X			X
Sweden	X	X	XX		
UK					X

X = evident XX = dominant

Source: EIRO

**8.20** Some countries are characterised by a general absence of coordination. The UK, France and Luxembourg have labour markets which are both decentralised and largely uncoordinated. These can be characterised by various combinations of: company-level bargaining, multiple-union representation within companies, competing pay claims between unions within and across sectors, and difficulties in enforcing contracts.

**8.21** A degree of coordination is, in a sense, imposed when a statutory minimum wage is set by legislation. This occurs in seven of the nine EU Member States which implement a minimum wage policy. Belgium and Greece are the exceptions, the minimum wage here being the product of binding national collective agreement.

**8.22** As Table 8.4 also illustrates, Belgium and Luxembourg are the only EU countries still to have automatic indexation (within the financial year) of pay and social security benefits (and, in Luxembourg, of pensions). In Belgium, indexation is triggered when the increase in the cost of living reaches 2 per cent; in Luxembourg, when the six month average increase reaches 2.5 per cent.

**Why the presence (or absence) of coordination matters**

**8.23** The degree of coordination among employer and employee organisations has important implications both for labour market flexibility and for the way in which labour market policy is implemented.

**8.24** When bargaining is highly centralised or coordinated, wages can be negotiated for a number of sectors. This may promote wage flexibility in aggregate; at the same time, however, it may inhibit relative wage flexibility.

**8.25** From a policy perspective, it is important to recognise that what constitutes a successful policy approach in a coordinated and highly consensual bargaining environment, may backfire in a more fragmented context and vice versa. Best practice from elsewhere must be adapted before it is 'imported'.

**8.26** Similarly, there is no single blueprint for the most appropriate application of labour market policy at an EU level. If institutional structures and dynamics differ, any one approach will produce very varied and unpredictable outcomes.

**8.27** Wages need to be responsive to local conditions. The dynamics of wage-setting, and the sensitivity of wages to changing economic circumstances, will naturally be affected by different labour market institutions and frameworks. Box 8.3 describes the Dutch ‘polder model’ an example of a highly consensual approach.

**Box 8.3: The Dutch ‘polder model’**

The **‘polder model’** is difficult to define, but characterised by a highly developed framework for consultation and an important role for social partners in decision making. Its workings can be seen in, for example, recent agreement within the **Social and Economic Council** (employers and trade union representatives, and independent ‘crown’ representatives) on reforms intended to cut the number of new disability benefit recipients each year from 80,000-100,000 to less than 30,000.

The **Labour Foundation** (Stichting van de Arbeid), established in 1945, is a consultation body of employers’ confederations and trade union confederations. Its main role is to shape the overall climate of industrial relations, and to act as an informal channel alongside the Social and Economic Council to advise the government on pay matters.

Pay bargaining itself is the prerogative not of the Labour Foundation, but of sector employer organisations. Collective agreements are regarded by the Ministry of Employment and Social Affairs as generally binding on an entire sector.

The consensual approach has its roots in the 1982 **Wassenaar accord** between employers, unions and the government, which delivered wage moderation in return for job creation. When the polder model works, it results in moderate wage growth and a low incidence of strikes. When it does not, it risks inertia, and has been criticised as having a negative effect on productivity, and as weakening the political system by extending the decision-making process and producing insufficient wage differentiation.

Twenty years on, calls have been heard for a new-style Wassenaar accord exchanging wage moderation for greater employer readiness to recruit from the ranks of the inactive (especially disability benefit recipients), and increased government spending on education, health and social welfare.

**More than just wages** **8.28** Collective bargaining has increasingly extended beyond wages and working conditions to embrace a range of other issues such as work-life balance, equal opportunities and, more recently, in some Member States, company pension contributions and funds. A broader agenda can be beneficial insofar as a tailored collective bargaining approach may be more acceptable to the parties concerned than a legislative or interventionist approach.

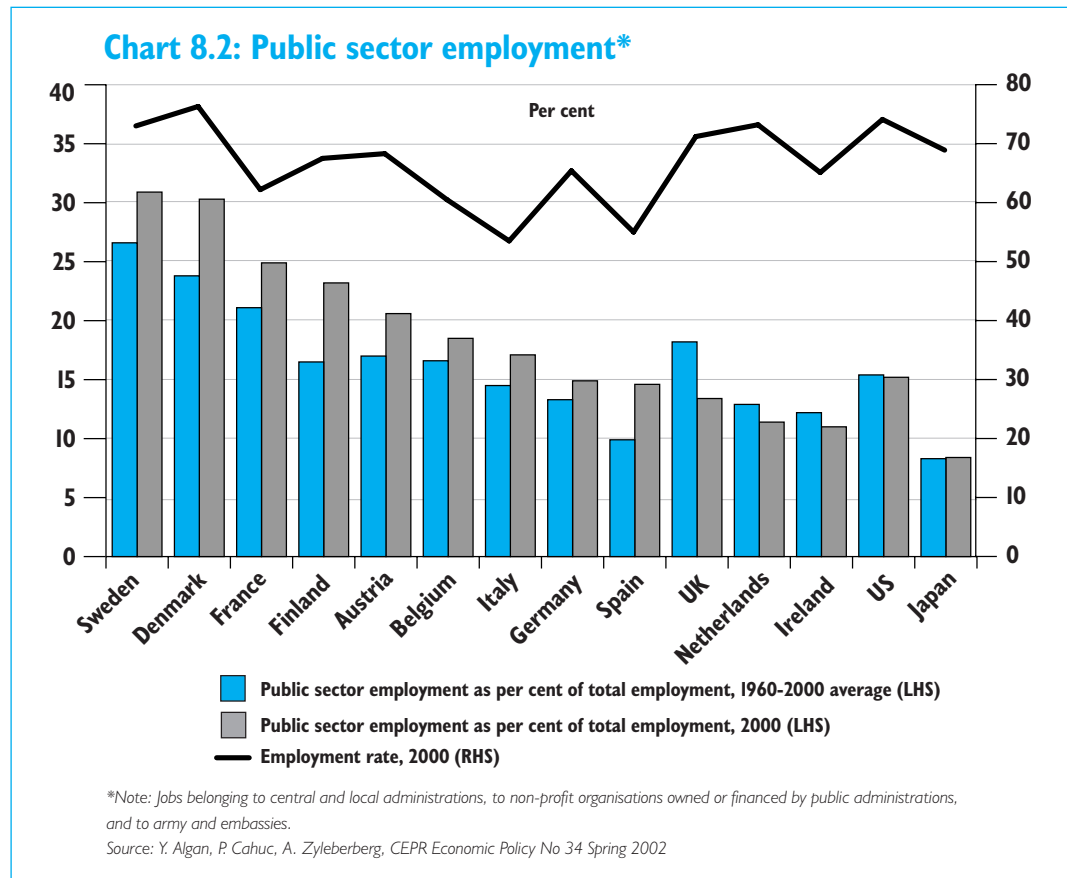
**8.29** Trade unions have also tended to take an increasingly flexible, or pragmatic, approach towards direct employee financial participation schemes. Profit-sharing and employee share ownership have been incorporated into collective agreements at both sector (e.g. Germany) and national (e.g. Ireland) levels.

**8.30** Employer organisations have on the whole been less active on this topic, opposing constraints on such schemes being offered, but regarding their application as a matter for individual employers. For them advantages include greater flexibility of remuneration, enhanced productivity and employee commitment, and possibly tax advantages. The schemes have, however, rarely been used as a means of introducing broad-based performance-related pay.<sup>4</sup>

<sup>4</sup>Recent trends in financial participation in the EU, European Foundation for the improvement of Living and Working Conditions, 1999.

**The public sector as employer** **8.31** The above description of wage bargaining frameworks is primarily a private sector story. Public sector bargaining tends, even in otherwise decentralised and uncoordinated systems, to be a rather more centralised affair and union density is commonly higher in the public sector.

**8.32** The public sector's share of total employment varies considerably between Member States and has tended to increase over time, as Chart 8.2 illustrates. Of the exceptions, an initially rising trend in the UK came to a halt in the 1980s and went sharply into reverse in the 1990s, while Ireland and the Netherlands saw relatively smaller declines, concentrated in the 1980s.



**8.33** Chart 8.2 also illustrates the lack of a link between the share of public sector employment, and total employment rates. A major role for the public sector as employer neither guarantees high employment nor precludes it.

**8.34** Some research does find a strong correlation over time between the size of public sector employment and the unemployment rate.<sup>5</sup> This might reflect a 'crowding out' of private sector jobs (if, for example, public sector employers competed with the private sector in output or labour markets, or if a larger public sector meant higher taxes on labour). Alternatively, however, government job creation could be a response to, rather than a cause of, rising unemployment.

**8.35** The potential labour market implications of the size of the public sector payroll are not, however, confined to the level of employment or unemployment, but include:

- the composition of employment, if the public sector is less discriminatory than the private in its recruitment and promotion of women, older workers, the disabled or ethnic minorities;

<sup>5</sup> *Public Employment and Labour Market Performance*, Y. Algan, P. Cahuc, A. Zylberberg, CEPR Economic Policy #34, Spring 2002.

- the government's ability to influence wage growth (both directly and by example);
- the extent to which the government can set an example with regard to, for example, work-life balance;
- the location and distribution of employment;
- the form of social dialogue; and
- the direct fiscal implications of wage growth and retirement patterns. France, for example, with a relatively large public sector, faces the pensions challenge over the coming years of a retirement boom among civil servants.

**Cross-border  
coordination in  
collective  
bargaining**

**8.36** Coordination between national trade unions or employers' bodies during a pay round is one thing; coordination on pay bargaining between unions or employers in different countries, quite another. Cross-border wage agreements are difficult to reach, for several reasons:

- pressure for more decentralised pay bargaining, from employers on the grounds of flexibility and efficiency, and from employees on the grounds of choice (in e.g. variable pay, working hours, leave arrangements);
- wage bargaining is still the prerogative of national, regional or local level negotiators, and organisational skills and bargaining strengths vary;
- bargaining cycles are not synchronised, and may vary from one to four years;<sup>6</sup>
- unions and employers in some Member States may give greater weight in framing their demands to, for example, corporate profitability, or qualitative aspects such as cuts in social security contributions or improvements in the welfare system;
- while coordinated pay claims generally assume an 'inflation plus productivity' formula, conventional measures of productivity, and the extent to which they are familiar bargaining elements, differ between Member States; and
- differing economic and political contexts will influence the objectives and relative strengths of both unions and employers.

**8.37** Notwithstanding these difficulties, cross-border coordination of collective bargaining has been pursued. (See Box 8.4 for a description of the inter-regional Doorn initiative, and Box 8.5 for sector coordination by European Industry Federations). While headway has been made in terms of a better exchange of information and understanding, this remains a long way removed from EU-level wage bargaining.

**8.38** Around 700 European Works Councils have been set up over the past fifteen years, but these rarely deal with the central issues in collective bargaining – pay, working time and working conditions. Some have, however, issued joint texts (including, on occasions, binding provisions) on e.g. gender equality, job security, employability and health and safety, or produced informal, unwritten agreements on issues such as share options, union membership or information technology.<sup>7</sup>

<sup>6</sup>IDS *Employment Europe*, February 2002.

<sup>7</sup>European Foundation for the Improvement of Working and Living Conditions.

**Box 8.4: Inter-regional coordination; Doorn, and union networks**

The Doorn Initiative, launched in 1997, represented a pioneering step in cross-border trade union coordination. It also represents the high water mark of such efforts. Representatives of major trade union confederations from Germany, the Netherlands, Belgium and Luxembourg agreed that collective bargaining settlements should 'correspond to the sum total of the evolution of prices and the increase in labour productivity', and that they would meet annually (with more regular meetings of an expert group) to evaluate past pay rounds and discuss future policy.

Table 8.5 illustrates the Doorn 'margin' and actual pay agreements for 1999-2001, as well as the working assumptions of the 2002 pay round. Germany followed 1999's high pay agreement with a very moderate two year pay round in 2000, leaving it (along with Belgium and the Netherlands, though not Luxembourg) undershooting its Doorn margin for the three year period.

That inflation and productivity forecasts are not always accurate means, of course, that the margin targeted may not in retrospect prove to have been appropriate. Furthermore, not everyone would accept the Doorn logic. German employers' associations, for example, declared at the start of 2002 that pay rises for the year should match only the rise in national productivity.

The Doorn agenda has broadened since its establishment. At the most recent annual meeting in September 2001, for example, it was agreed to incorporate lifelong learning into the 2002 bargaining round, and to explore the scope for joint cross-border campaigning on non-wage-related issues.

Most cross-border initiatives between individual trade unions tend not to encompass wage bargaining, but to be a response to the needs of members working overseas. Inter-regional collective bargaining networks (generally centred on or at least involving German trade unions) do, however, exist in such sectors as engineering, construction and chemicals. Each district organisation of German engineering union IG Metall has, for example, links with unions in other EU or candidate countries.

**Table 8.5: Agreed pay increases relative to the Doorn formula, 1999-2001 (per cent)**

		Inflation (A)	Productivity (B)	Doorn margin (A+B=C)	Agreed pay increase	Use of Doorn margin
Belgium	1999	1.1	1.2	2.3	3.0	0.7
	2000	2.5	2.4	5.0	3.4	-1.5
	2001	2.4	2.0	4.4	3.9	-0.5
	1999-01	6.1	5.7	12.2	10.7	-1.3
	2002	1.5	2.2	3.7		
Germany	1999	0.6	0.8	1.4	3.1	1.7
	2000	1.4	3.0	4.4	2.4	-2.0
	2001	2.5	0.9	3.4	2.1	-1.3
	1999-01	4.6	4.8	9.5	7.8	-1.6
	2002	1.3	2.3	3.7		
Luxembourg	1999	1.0	2.2	3.2	3.1	-0.1
	2000	3.2	2.2	5.5	5.1	-0.4
	2001	2.3	0.3	2.6	4.5	1.8
	1999-01	6.6	4.8	11.7	13.2	1.4
	2002	n/a	n/a	n/a		
Netherlands	1999	1.7	1.7	3.4	2.6	-0.8
	2000	2.1	2.0	4.1	3.3	-0.8
	2001	3.75	0.75	4.5	4.3	-0.3
	1999-01	7.7	4.5	12.6	10.5	-1.9
	2002	2.25	1.75	4.0		

Note: Trade union assumptions for 2002. Rows may not sum due to rounding

Source: Doorn Initiative Experts' Team

### Box 8.5: Sector coordination; European Industry Federations

Collective bargaining rarely featured on the agenda of most European Industry Federations (EIFs) until the late 1990s. An exception was the European Metalworkers' Federation (EMF).

The EMF had had a Collective Bargaining Committee since the 1970s, but began in the mid-1990s to give much greater weight to coordination. European collective bargaining guidelines were combined with 'EMF minimum standards' (on, for example, working time or training) as national bargaining objectives. Its approach remains more advanced than those of other EIFs; the Collective Bargaining Committee is now underpinned by a working party, a collective bargaining conference, an annual summer school, an information network and reporting system (EUCOB@), and inter-regional collective bargaining networks.<sup>8</sup>

Following the EMF's example, other EIFs have embarked down a similar road; in graphics; finance; mining energy and chemicals; textiles; public services; food, agriculture and tourism; building and woodwork; journalism; and transport.

#### Collective bargaining outcomes: recent decades

**8.39** While collective bargaining structures differ greatly across the EU, collective bargaining outcomes in terms of real wage growth have shown both long-term moderation and substantial convergence. As Table 8.6 shows, real wage growth (real compensation per employee less the GDP deflator) varied between 2.5 per cent and 7.1 per cent in the 1960s, but between only 0.2 per cent and 2.1 per cent in the 1990s.

<sup>8</sup> For further on EMF's approach, see *Europeanisation of Collective Bargaining*, T. Schulten, WSI Discussion Paper No. 101, May, 2002.

**8.40** Labour productivity growth (GDP per person employed) has also moderated and, in the 1980s and 1990s – and unlike in the 1970s – outpaced real wage growth.

**Table 8.6: Real wages and labour productivity growth, 1961-2000 (per cent)**

	1961-1970		1971-1980		1981-1990		1991-2000	
	Real Wages	Labour prod'y	Real Wages	Labour prod'y	Real Wages	Labour prod'y	Real Wages	Labour prod'y
Austria	4.6	5.1	4.2	2.9	1.6	2.2	1.1	1.6
Belgium	4.3	4.4	4.7	3.2	0.4	1.8	1.4	1.6
Denmark	3.9	3.4	1.6	1.6	0.5	2.0	1.7	2.2
Finland	3.7	4.4	3.6	3.2	2.5	2.6	1.4	2.8
France	4.9	4.9	3.6	2.9	1.1	2.1	1.1	1.6
Germany	4.6	4.2	2.9	2.6	0.8	1.7	1.4	2.0
Greece	6.3	9.3	3.2	3.0	0.1	-0.3	0.2	1.5
Ireland	4.1	4.2	4.2	3.7	2.1	3.8	1.4	3.2
Italy	5.9	6.2	3.0	2.6	1.0	1.6	0.1	1.5
Luxembourg	2.5	2.9	3.9	1.4	1.6	2.7	1.1	2.0
Netherlands	5.1	3.9	3.0	2.7	0.2	1.6	1.0	1.2
Portugal	6.6	6.2	5.6	4.7	1.4	3.0	2.1	2.1
Spain	7.1	6.7	4.6	4.2	0.7	2.2	0.7	1.3
Sweden	4.1	3.9	1.6	1.2	0.7	1.3	2.0	2.3
UK	2.7	2.6	1.7	1.6	2.2	2.2	1.6	1.8
EU	4.5	4.6	3.0	2.7	0.9	1.9	1.1	1.7

Source: EIRO, European Commission

#### EU-level dialogue and concertation

**8.41** While negotiation on wage claims is a primarily national affair, discussion and dialogue at an EU level occurs on a range of issues, having been kick-started by the ‘Val Duchesse’ process of 1985. This process was intended to foster EU-level dialogue between trade union and employer representatives, and has resulted in a number of joint statements on employment, education, training and other issues.

**8.42** Tripartite concertation (i.e. exchanges not only between both sides of industry, but also with the EU public authorities) is the rationale of the Standing Committee on Employment (SCE). This was reduced in size and reformed in 1999, in the context of the coordinated European employment strategy. Its employer and trade union organisation members<sup>9</sup> have, however, pressed for further reform, and presented a statement to this effect on the eve of the December 2001 Laeken summit. The Commission’s recent communication builds on this statement and proposes a new Tripartite Social Summit.<sup>10</sup>

**8.43** At an EU level, but within rather than across sectors, 27 sectors have, to date, established social dialogue committees (between employer and employee representatives). Dialogue took place in individual sectors in 2001 on a number of themes including equal opportunities, training, health and safety, corporate social responsibility, restructuring, the modernisation of work, teleworking and enlargement.<sup>11</sup>

#### An ‘EU model’ notable by its absence

**8.44** Industrial relations can – and, within the EU, does – take a variety of forms. Status rights which apply *de jure* in some countries, are achieved *de facto* in others through collective bargaining.<sup>12</sup> Similarly beneficial outcomes do not necessarily require similar processes and inputs, as the EU’s own labour market experience attests.

<sup>9</sup> The European Trade Union Confederation (ETUC), the Union of Industrial and Employers’ Confederations of Europe (UNICE), the European Association of Craft and Small and Medium-sized Enterprises (UEAPME) and the European Centre of Enterprises with Public Participation and of Enterprises of General Economic Interest (CEEP)

<sup>10</sup> *Communication on the European Social Dialogue; a Force for Innovation and Change*, European Commission, June 2002.

<sup>11</sup> European Industrial Relations Observations on-line, 4 February 2002.

<sup>12</sup> *The Europeanisation—or the Erosion—of Industrial Relations?* R. Hyman, *Industrial Relations Journal*, 32:4, September 2001.

**8.45** This chapter has focused on wage bargaining, bringing governments into the story primarily only insofar as they are employers or participants in tripartite pacts. Chapter 9 turns its attention to the other side of the industrial relations coin, labour market regulation, drawing into the analysis the importance also of product market regulation to labour market outcomes. In some Member States, such legislation is frequently the product of consensual negotiation; in others, of government fiat; and in all, to some extent, of decisions taken at an EU level. Once again, the 'EU model' is notable by its absence.

#### **Key Policy Questions**

- **Is the sheer diversity of national labour markets and the difference in approach to wage bargaining and social dialogue, sufficiently appreciated at both national and EU levels?**
- **Do trade unions and employer associations adequately reflect their members' interests? Do they take account also of the interests of 'outsiders'? Are these organisations therefore given too much or too little weight in policy formation?**
- **Is a compression of wage differentials being pursued at the expense of employment? Is less inequality in pay resulting in greater inequality of access to employment?**
- **In the public sector, should pay differentials reflect differences in the regional cost of living?**
- **Does the size of the public sector constrain or help a government in implementing labour market reforms?**
- **In which areas do the social partners consider that they can make a real impact towards the achievement of the Lisbon goals?**

**Summary**

- **Well targeted and designed regulation is of enormous benefit to citizens, businesses and the economy, by correcting market failures and ensuring increased fairness and safety.**
- **There is a range of tools with which to raise standards. Some involve legislation; others the promotion of best practice. Regulation is not always the answer. High employment protection legislation (EPL) is of little benefit if there is no employment to protect.**
- **The impact of EPL on employment levels is ambiguous. Insofar as it weighs more on some contracts and individuals than on others, it may alter the workforce composition; it may also affect pay demands and income distribution, and the average duration of unemployment.**
- **Cross-country differences in EPL have over the past decade, narrowed. Countries with higher levels of EPL have tended to deregulate, moving closer to the levels of their low EPL peers.**
- **Product market regulation also affects job creation, though regulatory ‘totals’ may not tell the whole story. Businesses, and especially SMEs and innovative companies, may be constrained far more by inward-oriented regulation than by barriers to trade or investment.**

**The benefits of regulation**

**9.1** Well targeted and designed regulation, complemented by effective policy on competition and state aid, is of enormous benefit to businesses and to the economy by correcting market failures, and to citizens through increased fairness and safety. Market outcomes do not always deliver, for example, the quality and safety which consumers demand. Policy intervention may be required in the form of standards, a more coherent analysis of the risks to consumers, tighter enforcement, or a better response to emergencies.

**9.2** Labour market regulation can enhance not only equity but, in several ways, efficiency. Laws regulating dismissal, or providing for income protection and maternity leave, help reinforce a relationship of mutual high commitment between employer and employee. This encourages both parties to invest in human capital, boosting the productivity not only of present employees but also – as the latter are then better placed to invest more in the health and education of their children – future generations.<sup>1</sup>

**9.3** Appropriate regulation can also help improve the quality of job-matching, and thereby reduce the cost of labour turnover to firms. And as UK experience illustrates, the introduction of a minimum wage not only need have no detrimental effect on employment, but may even boost participation and employment by ‘making work pay’. Decent standards in the workplace are not incompatible with efficiency.

<sup>1</sup> *The Design of Active Labour Market Policies: Building in effective incentives*, B. Cockx, International Labour Review Vol. 139, 2000.

**9.4** Not all regulation is, however, good regulation, and unnecessary or inefficient regulation carries serious costs. It restricts competition and stifles enterprise and new investment and, as a consequence, jobs. The European Commission has put the cost to the EU of badly drafted regulation at about €50 billion per year.<sup>2</sup>

**9.5** Badly targeted labour market regulation can have immediate and damaging effects. Labour market choice for both employers and employees on the one hand, and equity and security on the other must be kept in mind, and kept in balance. Employment protection rights are valuable, but of little value without employment

**9.6** At both a domestic and a European level, regulation must be transparent, accountable, targeted, consistent and proportionate to the problem it is intended to solve; and labour market regulation, in particular, has a difficult path to tread between adaptability and security.

### Comparing regulatory regimes

**9.7** Measuring and comparing different regulatory regimes cannot help but be somewhat subjective. Indices of labour market performance tend to focus on the degree of collective bargaining centralisation and EPL, but ignore the potential for law suits over discrimination or pension funds.

**9.8** Studies of the market-friendliness of product markets meanwhile, tend to count the number of hoops an entrepreneur must jump through to incorporate a new business and how many weeks this is likely to take, but forget differences in bankruptcy or other laws which can have an important influence on business formation and dissolution.<sup>3</sup> Only in the US, for example, do liability suits have the potential to bankrupt firms, or class action suits pose a major headache for businesses. At the same time, US bankruptcy law is particularly lenient in giving failed entrepreneurs another chance.

### Employment Protection Legislation

**9.9** EPL can be split into two broad categories:

- labour standards (e.g. sick pay, health and safety legislation, working time rules), which may influence overall costs, but do not directly affect the cost of hiring and firing; and
- employment protection in its strict sense, which may make both redundancy and hiring more costly.

### The impact on employment

**9.10** That high EPL constrains jobs growth and boosts unemployment, is a common but far from universally accepted argument. Empirically, cross-sectional regressions across countries tend to attach little significance to EPL and dismissal costs as a determinant of unemployment. Time-series analyses, in contrast, often find a positive relationship.<sup>4</sup> This may, however, be a reflection of the fact that governments faced with rising unemployment are likely to come under greater pressure from their electorates to legislate for greater levels of employment protection.

**9.11** A lack of correlation between EPL and unemployment<sup>5</sup> could, however, imply not that EPL has negligible consequences, but that it protects 'insiders' already in the labour market at the cost of pushing others not into unemployment, but into inactivity.

<sup>2</sup> *Internal Market Scoreboard*, European Commission, 2001. See also *Realising Europe's Potential; Economic Reform in Europe*, HM Treasury, March 2002.

<sup>3</sup> *What have two decades of British economic reform delivered?*, D. Card, R. Freeman, NBER Working Paper 8801, February 2002.

<sup>4</sup> *Anatomy of Employment Growth*, P. Garibaldi, P. Mauro, CEPR Economic Policy #34, 2002.

<sup>5</sup> *OECD Employment Outlook*, 1999.

**9.12** What of the argument that employment protection damages what it is supposed to protect – employment? The impact on jobs is somewhat ambiguous since, if the cost of labour force adjustment rises, both job creation and job destruction will fall. (This argument is consistent with smaller flows into and out of unemployment in the EU than in the US, but not with the EU’s comparably high gross job creation and destruction).

**9.13** High levels of protection may, however, have negative consequences for employment if they encourage employers to substitute capital for labour, or dampen firms’ incentives for capital accumulation and investment in new technology. This would constrain both economic and employment growth.<sup>6</sup> It can also have a disproportionate effect on low skilled or low productivity workers, as they are the most likely to be priced out of work by increases in non-wage costs.

**9.14** Inappropriately high EPL may make itself felt less on the level of employment than on the composition. This could occur in two ways:

- by affecting some types of contract more than others, EPL might alter the share of part-time or fixed term workers in total employment; and
- as EPL will tend to impact most strongly on individuals with an already weaker attachment to the labour market, the risk would be that it would dampen the employment presence of women, youths and older workers.

**...and on pay  
and  
unemployment**

**9.15** There could also be an impact on pay. Already employed ‘insiders’, now enjoying greater job security at the expense of non-employed ‘outsiders’, might feel encouraged to make higher pay demands. The income differential between those in work and those not in work would widen; so, too, might that between employees with the more ‘protected’ types of work contract, and employees without.

**9.16** Insofar as high EPL renders employers more reluctant to fill job vacancies, the average duration of unemployment could lengthen. This would imply a outwards in the Beveridge curve (which, as discussed in Chapter 6, links unemployment and vacancy rates).

**9.17** Reality, however, is often less clear-cut. UK experience during the 1970s, for example, suggests that higher EPL may prompt a more ‘professionalised’ personnel function within firms. If so, this may imply greater efficiency in job-matching, and hence simultaneous inward pressure on the Beveridge curve.<sup>7</sup>

**EPL rankings;  
narrower gaps**

**9.18** Table 9.1 shows comparative rankings of the strictness of EPL (it being assumed that the formal level of employment protection corresponds with the actual enforcement of legislation, which may not always be the case.) Higher values, on a scale of 1-6, imply greater protection.

**9.19** The ‘narrow’ measure is based on data for regular and temporary contracts; the ‘broad’ measure incorporates additional information on regulations covering collective dismissals. In some instances, such as New Zealand, this broader measure paints a considerably different picture to the narrower. In terms of assessing change, however, comparative data for the 1980s and 1990s are only available for the narrow series.

<sup>6</sup> *Anatomy of Employment Growth*, P. Gaaribaldi, P. Mauro, CEPR Economic Policy #34, 2002.

<sup>7</sup> *The Beveridge Curve; Unemployment and Wages in the OECD from the 1960s to the 1990s*, S. Nickell L. Nunziata, W. Ochel, G Quintini, Centre for Economic Performance LSE, October 2001.

**9.20** The US, UK and other English-speaking countries had, at the end of the 1990s, fewer restrictions than their neighbours on the rights of employers to adjust their workforces at will. The differences were, however, considerably smaller than a decade previously, due primarily to the more regulated countries having reduced their levels of EPL and narrowed the gap with their less regulated peers.

**Table 9.1: Employment protection indices**

	Late 1980s (narrow)	Late 1990s (narrow)	Late 1990s (broad)	Change, late 1980s-1990s (narrow)
Austria	2.2	2.2	2.3	0
Belgium	3.1	2.1	2.5	-1.0
Denmark	2.1	1.2	1.5	-0.9
Finland	2.3	2.0	2.1	-0.3
France	2.7	3.0	2.8	0.3
Germany	3.2	2.5	2.6	-0.7
Greece	3.6	3.6	3.5	0
Ireland	0.9	0.9	1.1	0
Italy	4.1	3.3	3.4	-0.8
Neths	2.7	2.1	2.1	-0.6
Portugal	4.1	3.7	3.7	-0.4
Spain	3.7	3.1	3.1	-0.6
Sweden	3.5	2.1	2.6	-1.3
UK	0.5	0.5	0.9	0
Australia	0.9	0.9	1.2	0
Canada	0.6	0.6	1.1	0
Japan	n/a	2.4	2.3	n/a
New Zealand	n/a	2.6	0.9	n/a
Switzerland	1.0	1.0	1.5	0
US	0.2	0.2	0.7	0

Note: The 'narrow' measure represents protection for regular and temporary contracts; the 'broad' measure takes account also of collective dismissal legislation

Source: OECD Employment Outlook, 1999, cited in 'What Have Two Decades of British Economic Reform Delivered?' D. Card, R. Freeman, NBER Working Paper 8801, February 2002.

**9.21** As Table 9.2 shows, the number of reforms undertaken by Member States to make EPL more well-designed or to increase the attractiveness of employment (relative to non-employment) was considerably larger in the latter half of the 1990s than in the preceding ten years.<sup>8</sup>

**Table 9.2: Number of labour market reforms in the EU**

	Number of reforms reducing strictness of EPL	Number of reforms increasing returns to employment
1986-94	16	32
1995-01	24	61

Source: P. Garibaldi, P. Mauro, CEPR Economic Policy No.34, 2002.

**9.22** Such an overview does not allow for the quality or intensity of the measures, nor does it allow for reforms which may have headed in the opposite direction. Nevertheless, the picture is certainly consistent with a more employment-friendly Europe at the end of the decade than at the beginning.

<sup>8</sup> *Anatomy of Employment Growth*, P. Garibaldi, P. Mauro, CEPR Economic Policy No.34, 2002.

**9.23** An exception to the deregulatory trend of the above tables has been France, which during the 1990s added extra layers of employee protection. At the same time France ended the decade with accelerating jobs growth (around 1.6 million new jobs between 1997 and end-2000) due to both stronger economic growth and an increase in the employment content of growth.

**9.24** This does not, however, mean that higher levels of EPL are better for employment, and not only because the impact of such major recent changes as the shorter working week and the social modernisation law have yet to be gauged. The French labour market remains comparatively illiquid, a low rate of job loss combining with a low rate of re-entry into employment to leave employment vulnerable to economic or technological shocks.<sup>9</sup> Furthermore, analysis suggests that, while strong social regulation has impeded the development of wage inequality, new forms of inequality have emerged in its place; in particular, inequality of access to unemployment, concentrated at the lower end of the income scale.<sup>10</sup>

**Product market regulation and labour markets**

**9.25** Not every piece of legislation that has an impact on employment is targeted directly at labour markets; product market legislation, competition policy and health and safety legislation can all have important effects. Product market legislation can help increase competitive pressure among existing firms, affect how quickly economies can adjust to shocks, reduce firms' market power, and the wage premium commanded by workers in those firms, reduce entry costs for new companies, and stimulate entrepreneurship.<sup>11</sup>

**9.26** Product market regulations can be grouped into two categories: 'inward oriented' regulations, such as state control of industry, barriers to entrepreneurship, and regulation of domestic markets; and 'outward-oriented' regulations, which cover barriers to trade and investment. Table 4.11, using data from the OECD's database of around 1300 such regulations, summarises aggregate measures of the regulatory burden in each category and in total. Higher scores indicate a thicker and more intrusive regulatory system. (Note that these data relate to 1998, and that national circumstances may in some cases have changed in the interim.)

**9.27** The UK, Ireland, Australia and the US have, on OECD estimates, the lightest level of product market regulation (the UK, in particular with regard to domestically oriented measures). That Member States tend to lean more towards inward-oriented regulation than their non-EU counterparts, may be in part a reflection of EU membership itself. The scope for erecting national barriers to trade and investment is clearly constrained by membership of a Single Market, and especially of one including most major trading partners.

**9.28** Countries with comparable regulatory totals in Table 9.3 will not necessarily see comparable performance on employment. Businesses, and especially SMEs and innovative companies, may be hindered or discouraged far more by inward-oriented regulation than by barriers to trade or investment (though the latter will clearly have some influence).

<sup>9</sup> *Plein Emploi*, Conseil D'Analyse Économique, December 2000.

<sup>10</sup> *Inégalités Économiques*, Conseil D'Analyse Économique, July 2001.

<sup>11</sup> *Product and labour market interactions in OECD countries*, G. Nicoletti, A. Bassanini, E. Ernst, S. Jean, P. Santiago, P. Swaim, OECD Working Paper No.312, December 2001.

**9.29** Belgium has a lower regulatory total score than Norway, and a broadly comparable reading to Finland and Switzerland. Given, however, that it leads all three in terms of its domestically-oriented score, Belgian businesses in the late 1990s might have felt themselves rather more hamstrung by product market rulings than their regulatory total would suggest – and more constrained, also, than their Finnish and Swiss counterparts.

**Table 9.3: Indices of product market regulation, 1998**

	Inward-oriented	Outward-oriented	All
Austria	118	54	140
Belgium	270	63	190
Denmark	190	54	170
Finland	230	63	190
France	270	103	210
Germany	190	54	140
Greece	270	132	220
Ireland	80	43	80
Italy	330	49	230
Netherlands	180	54	140
Portugal	210	107	170
Spain	220	68	160
Sweden	170	84	140
UK	50	43	50
Australia	120	43	90
Canada	100	215	150
Japan	180	102	150
New Zealand	140	95	130
Norway	220	215	220
Switzerland	220	132	180
US	110	87	100

Source: Nicoletti, Scarpetta and Boylaud, 2002<sup>12</sup>

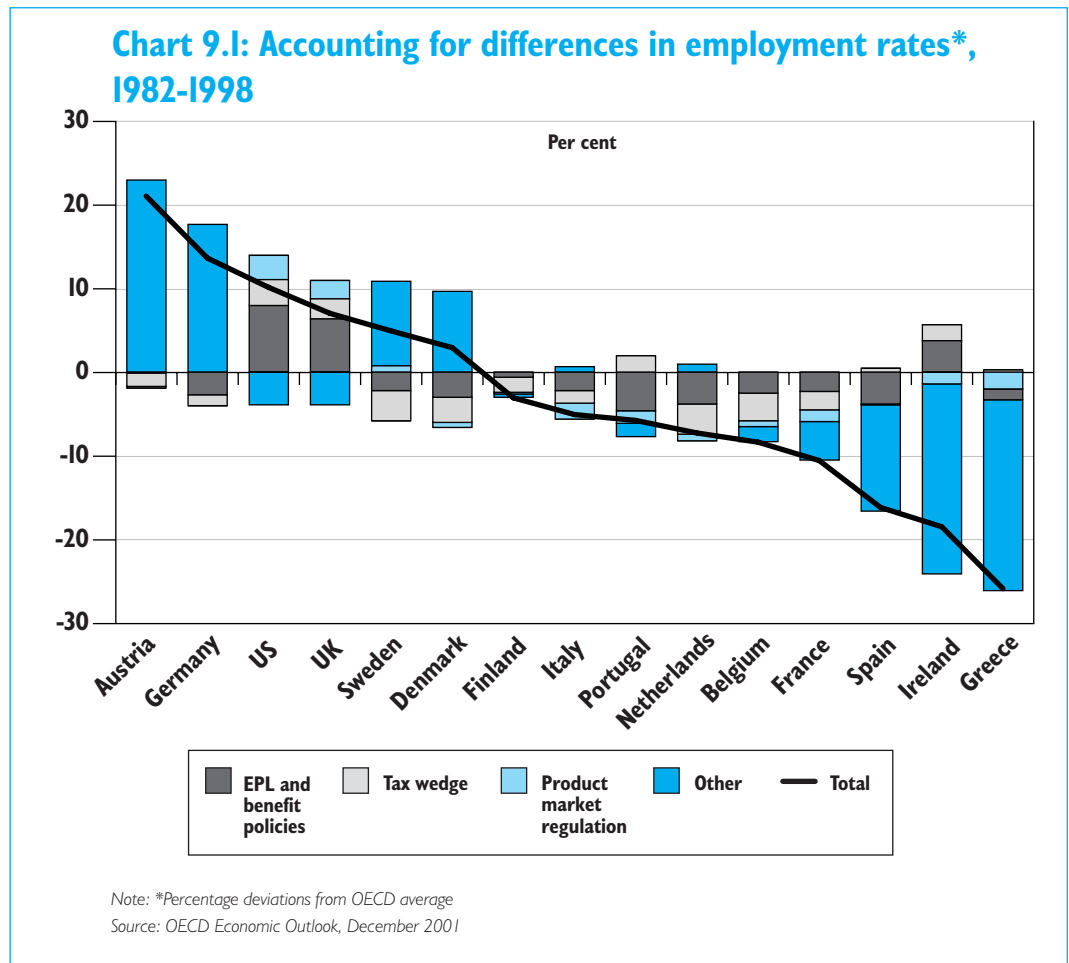
**EPL and product market regulation combined**

**9.30** The OECD<sup>13</sup> has explored the extent to which differences in employment rates over the period 1982-1998 can be attributed to EPL and benefit policies, to product market regulation, to the tax wedge, or to ‘other’ factors<sup>14</sup> (with the last accounting for about 60 per cent of total variation). The results for EU countries and for the US are shown in Chart 9.1.

<sup>12</sup> See *What Have Two Decades of British Economic Reform Delivered?* D. Card, R. Freeman, NBER Working Paper 8801, February 2002.

<sup>13</sup> OECD Economic Outlook, December 2001.

<sup>14</sup> Bargaining systems, unionisation, output gaps, country-specific effects and residuals.



**9.31** Labour market policy settings account, in general, for the major part of the 40 per cent of the variation in employment rates that can be explained, but the analysis also confirms the significance of product market settings. OECD-wide, differences in product market regulation accounted for just over 1 percentage point of the cross country differences in employment rates. This was equivalent to half the deviation attributable to the tax wedge, and a third of that explainable by EPL and benefit policies.

**9.32** As the chart shows, however, such overall figures conceal substantial variation at a Member State level. In Italy and Greece, for example, product market regulation weighed relatively heavily on employment rates, while UK and US employment benefited from light product market regulation. The level of EPL was a dampener to employment in Portugal, the Netherlands and Spain, but a boost to it in the US and UK. The size of the 'other' component also varied substantially, being particularly large and positive in Austria and Germany, but a large negative in Greece and Ireland.

**The joint dynamics of legislation and collective bargaining**

**9.33** Legislation and collective bargaining are two sides of the industrial relations coin. While we have separate chapters in this paper on each, each in practice influences the other, and their combined dynamics can have very different implications for economies and for policy makers.

**9.34** Some academic research suggests, for example, that in a high EPL economy, innovation and R&D may be stronger when there is a high degree of coordination among employers and unions, than when coordination is low.<sup>15</sup> High tech firms, in particular, demand a constant upgrading of the skills of their workforce. Bargaining frameworks which encourage this to be done internally via training are advantageous when legislation makes labour force adjustments difficult; when EPL is high, a highly coordinated bargaining system may cope better in some respects than a less coordinated system (which is not an argument for a high level of EPL per se).

**9.35** Where, however, the labour market is characterised by a lack of coordination, skills upgrading may occur to a greater extent through the open labour market. Employers are more likely to bid for appropriately skilled labour; wider pay differentials give employees the incentive to train. An uncoordinated labour market therefore puts a greater premium on job turnover and hiring flexibility; its efficiency, effectiveness, and contribution to innovation and growth may be much more damaged by strict EPL than would a more coordinated bargaining model.

**9.36** The institutional, bargaining and regulatory framework of an economy cannot help but influence the way in which policy is most effectively delivered. Different national contexts mean that realising similar objectives may often require different policy approaches; and it is to the important issue of policy recommendations that the final chapter now turns.

#### **Key Policy Questions**

- **Does EPL facilitate different working practices, or does it distort employee and employer choice?**
- **In formulating, communicating and implementing EPL, is sufficient account taken of the particular time and resource constraints affecting small businesses?**
- **Do low employment rates for particular social groups reflect too little EPL, or too much?**
- **Is regulation in the product or capital markets stifling business start-ups, expansion and innovation, and hence employment growth?**
- **Is regulation properly evaluated? Do the benefits outweigh the costs?**
- **Is legislation properly explained and understood, in terms of the rationale, the requirements, and the penalties for non-compliance?**
- **Does widespread ‘irregular’ economic activity point to overly rigid regulation?**

<sup>15</sup> *Product and labour market interactions in OECD countries*, G. Nicoletti, A. Bassanini, E. Ernst, S. Jean, P. Santiago, P. Swaim, OECD Working Paper No.312, December 2001.