Unemployment and Welfare State Reform: The Lisbon Agenda

Picking up any major European newspaper, one will not have to look far to find a story, editorial, or opinion piece about the linked problems of unemployment and welfare state reform. Dig deeper (or read further) and it is easy to find polemics criticizing the European Union for failing to respond adequately to the "jobs crisis". Deeper still and the implication lying beneath much European newspaper commentary is that – far from making the employment situation any better – European integration has only made matters worse.

When an argument is layered like this in the media, it is often too easy to agree with the analysis. Fingers wag, tempers rise, opinions harden, and decisions are made. Post referendum Eurobarometer polling suggests that this is what happened to the French electorate. When the European Constitutional Treaty was put up for ratification in a popular referendum held on May 29, 2005, 55 percent of French voters rejected the treaty. Of these, 31 percent said they voted against the treaty because they feared it would lead to further unemployment, 26 percent said it was because there was already too much unemployment in France, and 19 percent said it was because the treaty would lead to neoliberal reforms of welfare state and market institutions. The fact that the treaty contained very few (very minor) revisions to the economic institutions of the European Union did not matter at all.

The French veto of the European Constitutional Treaty serves as just one example of how unemployment and welfare state reform are problems with vast implications. The weakness of European economic growth rates, the volatility of European electorates, the rise of extremist political parties on the right and the left, and the heightened salience of issues like immigration, multiculturalism, and racial or religious intolerance all can be traced back to the same juxtaposition of unemployment and welfare state reform. Europeans feel insecure in their employment, they fear job loss from foreign competition and from foreign workers, and they resist efforts to cut back on entitlement provisions or labor market regulations that they believe will make them worse off (even if they are willing to acknowledge that such reforms will make markets work better).

Not all big problems require big solutions. Unemployment and welfare state reform are concerns across Europe. Many jump to the conclusion that Europe must be the response to these concerns, or, if not the response, then Europe must be the cause. However, such thinking is incorrect. Most economists agree that unemployment is a problem that can only be tackled at the local and regional levels. Unemployment rates vary as much within European countries as they do across countries in Europe. According to Eurostat data for 2006, unemployment within the EU ranged from 3.9 percent in Denmark to 13.4 percent in Slovakia. Unemployment in Germany ranged from 6.3 percent in Baden Wuerttemberg to 19.2 percent in Mecklenburg; in Italy it ranged from 3.6 percent in the Northeast to

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12.7 percent on the islands; and in Spain it varied from 6.3 percent in the Northeast to 12 percent in the South. By the same token, welfare state reform is a task of the member states and not the European Union (EU). Any obvious connection between the issues of unemployment and welfare state reform varies from one country to the next. Different institutions – whether for unemployment insurance, old age pensions, health care, education, hiring or firing – have different pathologies, they create different incentives, and they cause different problems for firms working in different countries.

The causes of unemployment are similarly varied and usually local or global, rather than European. Hence, finding a common solution to the problem of unemployment is no more realistic than looking to cure the common cold. Finding a universal formula for the pattern for welfare state reform is unrealistic as well. Nevertheless, the expectation that the EU offers some sort of panacea for these problems is widespread and widely encouraged. A Eurobarometer poll released shortly before the June 2004 elections for European Parliament revealed that almost 60 percent of potential voters believed employment to be the most important issue in the election campaign – far more than any other issue. The European Commission president, José Manuel Barroso, placed job creation at the center of his work program. And successive European Council presidencies – including, in particular, the British – have focused the lion's share of their attention on driving forward the process of welfare state reform.

Four questions emerge from the juxtaposition of these issues: Why is the EU held responsible – and why do EU politicians accept responsibility – for a combination of policy issues which "Europe" cannot resolve? What will happen if, as expected, Europe fails to address the problems of unemployment and welfare state reform? How can the worst case scenarios be avoided? And why should we try?

Initiative

The European Union's responsibility for employment dates back to the early 1990s, when the Delors Commission issued a White Paper on jobs, growth, and competitiveness. The White Paper was written to address the malaise that set in during the immediate aftermath of the Maastricht Treaty negotiations. Although there had been much euphoria surrounding the transformation of the European Community into a European Union, the economic downturn of the early 1990s quickly sapped away support. The Delors Commission (and the Belgian presidency of the European Council) hoped that a strong declaration on improving European economic performance would help make European integration seem more relevant to the major economic issues of the day.

As the 1990s progressed, and Europe's major economies continued to perform badly, initiatives to link integration with competitiveness and job creation began to multiply. Moreover, they became entangled – somewhat defensively – with the progress of monetary integration. When critics tried to blame the poor state of economic performance on fiscal consolidation or disinflation measures required to join the single currency (the

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euro), European politicians responded that integration is part of the solution to the jobs crisis, and not part of the problem. The more efforts countries made to qualify for participation in Europe's monetary union, the stronger the rhetoric became about the importance of Europe's contribution to economic performance.

The June 1997 Amsterdam Treaty marked a watershed in this development. On the one hand, the European Council made a pact to maintain macroeconomic stability and to foster growth by forging disciplined policies for taxation and spending (the "Stability and Growth Pact"). On the other hand, the European Council adopted a new provision to the Treaty Establishing the European Community giving Europe formal responsibility for the promotion of employment ("Title on Employment"). Of the two agreements, the Stability and Growth Pact was widely regarded by students of European integration as the more significant. Economists have long argued that fiscal discipline is an important component of monetary integration, and Europe's largest member state, Germany, was the motive force behind the Pact. By contrast, the Title on Employment was viewed as an empty concession made for newly installed left-wing governments in France and Britain, or as a further bribe to stimulate popular support.

Expectations

Despite the low expectations attached to the Title on Employment, efforts to make European integration more relevant as a solution to the jobs crisis soon gathered steam. In November 1997, the European Council convened a special summit in Luxembourg to encourage the member states to coordinate their efforts to encourage job creation. The European Council met again in Cardiff the following June (1998) to examine how Europe could stimulate supporting reforms for labor, capital, and goods markets. And in June 1999, the European Council met yet again to seek ways to bring both trade unions and employers into efforts at job creation and market-structural reform.

In each of these cases, the European Union played at most only a supporting role. Both politicians and policymakers consistently acknowledged that unemployment is a local and regional problem and that welfare state reform is a national prerogative. Yet as the performance of Europe's largest economies began to improve, belief in the value of this supporting European effort suddenly increased. Going into March 2000, expectations about the contribution Europe could make in resolving the jobs crisis surged ahead of its record of achievement. The European Council meeting at Lisbon declared the strategic objective of transforming Europe into the world's most competitive and dynamic knowledge-based economy. Moreover, it announced that it would achieve this goal through a new "open method of coordination" – combing the various job-creation and market reform processes into a single strategy for promoting flexible economic adaptation in the EU member states. Finally, the newly announced "Lisbon strategy" included a fixed time-frame for achievement. Europe would tackle both unemployment and welfare state reform by 2010.

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Achievements

The Lisbon strategy became an overnight success – both rhetorically and institutionally. Politicians fastened the 2010 target date as a means of galvanizing political support for welfare state and labor market reforms. Most prominently in Germany, but elsewhere as well, 2010 began to take on much of the same symbolic significance in the European reform process that the 1992 deadline had held for the completion of the single internal market. Meanwhile policymakers (and policy analysts) began to promote the open method of coordination as a means for addressing an ever wider array of issues. What started as a technique for promoting job creation and market liberalization soon extended a host of policy issues ranging from on the job training, to continuing education, gender equality and social exclusion.

The success of the Lisbon strategy was less evident, however, in terms of macroeconomic performance. On the contrary, the economic downturn that started at the end of 2001 and deepened in 2002 quickly reasserted the limits of European influence on labor market performance. As economic stagnation continued in 2003 and 2004, the progress of welfare state reform ground to a halt as well. Once exemplary reform countries, such as the Netherlands and Great Britain, suddenly became subjects for renewed concern. The situation for less exemplary countries, like France and Germany, was even worse. The European Council meeting in March 2004 called for a mid-term review of the Lisbon strategy to be carried out in two phases, with a group of senior political figures meeting under the chairmanship of former Dutch Prime Minister Wim Kok to produce a report that could feed into the European Commission's own analysis.

When the Kok Group reported its findings in November 2004, the result was a fundamental condemnation of Lisbon's apparent success. Kok argued that the 2010 deadline was unattainable (and, implicitly, that the strategic goal of creating the world's most competitive and dynamic knowledge-based economy was unrealistic). He also explained that much of the failure was due to the over-extension of the open-method of coordination and to a lack of clearly identified priorities for member state action to achieve. Rather than trying to achieve everything at once, Europe's politicians and policymakers should set out which goals are the most important and then focus all of their efforts on making progress. The Kok report concluded that no less than the sustainability of the European social model was at stake.

Limitations

The Kok report and the subsequent mid-term review of the Lisbon strategy reasserted the importance of finding a solution to the linked problems of unemployment and welfare state reform. However, aside from emphasizing that these problems should be given priority, neither the Kok report nor the mid-term review could offer a clear and effective European solution. Instead, both acknowledged that "European" responses are fundamentally dependent upon decisive action to be taken by the EU member states.

The two reports together have done much to reestablish the original motivation behind the Lisbon strategy. However, they leave two problems unaddressed. First, the European electorate expects a European solution to European unemployment. Moreover, if anything the rhetoric surrounding the Lisbon strategy reinforces that expectation. Second, with the manifest failure of the Lisbon strategy, the member states have lost much of the political impetus for undertaking domestic reforms. The 2010 deadline no longer serves to galvanize public opinion, and the open method no longer results in much coordination.

These two problems are not only difficult to resolve on their own; they are also mutually reinforcing. As reform progress slows down, unemployment continues to mount. Meanwhile, short-term unemployment becomes long-term unemployment, disaffected workers drop out of the labor market, and economic inequality and social exclusion become ever larger problems in their own rights. The effects are most readily apparent in the fiscal accounts of the various member states. Where once all EU member states pledged to maintain government taxation and spending close to balance or in surplus as part of the Stability and Growth Pact, by 2005 almost half of the EU's then 25 member countries had deficits in excess of 3 percent of gross domestic product – which are clearly defined as "excessive" in the language of European treaties. The reasons for such imbalances lie on both sides of the accounting: slow growth and low employment depress government revenues; high unemployment, inequality, and social exclusion raise outlays.

Solution

The European solution to the linked problems of unemployment and welfare state reform builds on three different actions. First, European politicians had to accept responsibility for these problems at the national level – explaining that "Europe" cannot be held accountable for what the member states have failed to do. This was politically complicated, to say the least. But it was necessary to shield EU institutions from the unrealistic expectations that have been fostered in the past. Second, EU politicians had to explain the real benefits of coordination at the European level. It is not enough to say that "Europe" cannot be held responsible for European unemployment; it is also necessary to explain how European-level coordination can help prevent solutions for one member state from causing problems for another, how they can help countries learn from their own successes and failures, and how they can diffuse conflicts between the winners and losers from change. This has proven more difficult to accomplish. Third, it was vital that European politicians recast the debate about welfare state reform (and the solution to European unemployment) as matters of progress and not survival. The alarmist message of the Kok report has done more to harden positions against reform than to promote any enthusiasm for further change. Yet there is much to celebrate in the rising level of productivity in the workplace, the wider variety of goods and services that are on offer, the rising standards of living (and life expectancy) across society as a whole, and the possibilities for all parts of the workforce to achieve more meaningful and less physically demanding positions of employment. Europe's economies are being challenged by the fruits of their own success. And few would willingly give up those benefits, even if that

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sacrifice were to provide a lasting solution to the problems that unemployment and welfare state reform entail.

The recasting of the Lisbon strategy after March 2005 accomplished much of this new agenda. The European Council pushed responsibility for welfare state reform back onto the member states – calling upon them to draft national programs that could be used as the basis for measuring national achievements. Although these national programs were not as ambitious as the original Lisbon strategy itself – and none could pretend to build the world's most competitive and dynamic knowledge based economy by the end of the decade – they did effectively underscore the national ownership of national reforms. Where the new Lisbon strategy has not succeeded, however, is in explaining what the European Union's role is in these national reform efforts. Perhaps it does not have to do so. In the intervening period, European economic performance has improved and unemployment has retreated. Government fiscal positions strengthened as well, such that virtually all member states were in compliance with the rules on excessive debts and deficits by early 2008. And while there remains much to be done in order to prepare Europe's welfare states for the economic and demographic challenges of the future, there is less concern that nothing can be accomplished (and guarded optimism that progress is being made).

Given this recent turn of events, it is possible that the solution for welfare state reform in Europe is not too far removed from the more general economic situation in the United States – both by example and by implication. No institutions are perfectly configured and no markets perfectly efficient. There is always room for improvement and the necessity for reform. Whether or not the European Union succeeds in solving its linked problems of unemployment and welfare state reform, the United States would do well to learn from Europe's example. If it does not, there is always the danger that poor economic performance in the United States could drag down the European economy as well. This would not only weaken welfare state reform efforts at the member state level, but could also bring the European Union's role in solving the "jobs crisis" again to the fore.

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