Quo Vadis Europe?

ECONOMIC EFFICIENCY VERSUS SOCIAL EQUALITY? The U.S. Liberal Model versus the European Social Model

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This article begins by challenging the widely held view in neoliberal discourse that there is a necessary trade-off between higher efficiency and lower reduction of inequalities: the article empirically shows that the liberal, U.S. model has been less efficient economically (slower economic growth, higher unemployment) than the social model in existence in the European Union and in the majority of its member states. Based on the data presented, the authors criticize the adoption of features of the liberal model (such as deregulation of their labor markets, reduction of public social expenditures) by some European governments. The second section analyzes the causes for the slowdown of economic growth and the increase of unemployment in the European Union—that is, the application of monetarist and neoliberal policies in the institutional frame of the European Union, including the Stability Pact, the objectives and modus operandi of the European Central Bank, and the very limited resources available to the European Commission for stimulating and distributive functions. The third section details the reasons for these developments, including (besides historical considerations) the enormous influence of financial capital in the E.U. institutions and the very limited democracy. Proposals for change are included.

I. THE ECONOMIC EFFICIENCY OF THE LIBERAL MODEL (U.S.) VERSUS THE SOCIAL MODEL (E.U.)[1]

Is It Valid to Compare the Economic Efficiency of the United States and the European Union?

One of the most influential positions reproduced in economic, financial, and political liberal circles on both sides of the Atlantic is that there is an intrinsic

[1] This section relies heavily on Navarro and Schmitt (1).

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conflict between economic *efficiency* and *reduction of inequality.* As proof of this position, liberal authors hold up the United States as an example of economic *efficiency* (with high economic growth and low unemployment), assumed to have been achieved by tolerating levels of social inequality (the United States has the highest level of income inequality in the Organization for Economic Cooperation and Development) that the European Union would not accept. The low economic growth and high unemployment of the European Union are considered to be a consequence of an excessive concern with equality, a concern that is evident in the European Union's extensive welfare states and its highly regulated labor markets. This idea of a trade-off in *efficiency* and *equality* is almost dogma today in many liberal circles.

As with many dogmas, however, this liberal dogma is reproduced more by faith than by evidence. But before we present the evidence that questions such a trade-off, we should make some observations about a reality that is frequently ignored in comparisons between the United States and the European Union. The first observation is that, when we compare the United States with the European Union, we are not comparing apples with apples but, rather, apples with oranges. The United States is a federal state with a federal government that has its own economic, social, and fiscal policies. The European Union, however, is primarily an aggregate of 15 nations/states (E.U.-15; recently increased to 25), each with its own economic, social, and fiscal policies. Therefore, to compare the United States with the European Union is not a rigorous project from a scientific point of view. The differences between the United States and the European Union are enormous. To start with, the U.S. federal structure differs substantially from the institutions of government of the European Union. Moreover, the federal government manages 19 percent of the U.S. GNP (gross national product; total U.S. public expenditures represent 30 percent of GNP), enabling the federal government to intervene actively in the management of the economy. (Contrary to what is assumed by many liberal authors, the U.S. federal government is enormously interventionist, shaping large components of research and development in its economy, to mention just one example.) This federal interventionism also allows for active correction of the regional inequalities that exist in the United States.

The European Union, however, does not have a federal government. The "E.U. budget" controlled by the E.U. Commission controls only 1.27 percent of the entire European GNP—a dramatically insufficient amount to have any impact as a stimulant for economic growth or as a corrective for regional inequalities within the European Union, regional inequalities that are, incidentally, much larger in the European Union than in the United States. The unemployment rate differentials between the U.S. regions with highest unemployment and those with lowest unemployment are much lower (7.0 percent in the state with the highest unemployment vs. 3.2 percent in the state with the lowest unemployment) than in the European Union (32 percent vs. 3.8 percent).

Another major institutional difference between the United States and the European Union is the pattern of influences and functions of U.S. institutions versus E.U. institutions. The U.S. Central Bank (the Federal Reserve Board) has a different objective and modus operandi than the European Central Bank, a difference we will expand upon later. These and many other institutional differences greatly limit the comparisons that can be made of the economic efficiency of the U.S. model versus the E.U. model, limitations that become even more apparent when the assumed differences in economic efficiency between the two continents are attributed—as they are by liberal authors—to differences in their labor markets or in the extent of their welfare states, while ignoring the institutional differences that are of paramount importance.

Based on these observations, it would be more reasonable and logical to compare U.S. economic efficiency with the economic efficiency of national states in Europe such as Germany, France, and Italy, among others, or with the Scandinavian countries. If that were done, it could be shown that governments such as those of the Scandinavian countries (which have been governed for long periods of time since World War II by political parties belonging to the social democratic traditions and which have followed policies opposite to liberal ones) have overseen higher levels of well-being and quality of life of their populations and have been more efficient economically (with greater competitiveness) than the United States. Even the liberal World Economic Forum (also known as the Davos Forum) has recognized (in its latest Report on Competitiveness) these Scandinavian countries as among the most competitive in the OECD (Finland ranked number 1; Sweden, 3; Denmark, 5; Norway, 6; Iceland, 10). Based on these data, it would seem that the logical place for the European Union to look for an economic model should not be to the United States but, rather, to the Scandinavian countries.

Which Has Had Higher Economic Growth: The United States or the E.U.-15?

The slow economic growth of the E.U.-15 versus the high economic growth of the United States is a constant reference point in liberal discourse. As proof of the major economic efficiency of the United States, liberal authors cite the rate of growth of the U.S. and the E.U. economies during the period 1975–2000. And the data they show seem to prove them right. Dividing the period 1975–2000 into four periods (1975–1985, 1985–1990, 1990–1995, and 1995–2000), we can see that the rate of economic growth for each period is superior in the United States (3.4, 3.2, 2.4, and 3.3 percent) than for the same periods in the E.U.-15 (2.3, 3.2, 1.5, and 2.3 percent).

What those liberal authors (and many others) ignore, however, is that, from these data, one cannot derive the conclusion that the United States is more efficient economically than the E.U.-15. The higher rate of economic growth of the United

States is due more to its larger demographic growth (in each of the four periods) than to its assumed larger economic efficiency. Actually, when we analyze *the rate of economic growth per capita,* we can see that the rate is similar on both sides of the Atlantic. During the period 1981–1990, for example, the growth rate per capita was 2.1 percent for the E.U.-15 and 2.2 percent for the United States; for the period 1991–1995, the rate for the E.U.-15 was 1.2 percent, slightly higher than the 1.1 percent rate for the United States; and for the period 1996–2000, the rate for the E.U.-15 was 2.4 percent, only slightly inferior to the rate for the United States at 2.8 percent. In reality, the rates of economic growth per capita have been very similar since 1980, and in fact were much larger in the E.U.-15 than in the United States prior to 1980 (during the period 1960–1980).

But if, rather than comparing the United States with the entire E.U.-15, we compare it—as we should—with individual countries in the E.U.-15, we can see that U.S. economic growth per capita during the 1980s was similar to the growth in the majority of countries of the E.U.-15, and inferior to several of them (U.S. 1.9 percent, about equal to or smaller than Austria, 2.1 percent; Belgium, 1.9 percent; Ireland, 6.6 percent; Netherlands, 2.4 percent; Portugal, 3 percent; Spain, 2.4 percent; and Denmark, 1.8 percent). All these countries have more regulated labor markets and larger welfare states than the United States, and therefore it cannot be said that the economic efficiency of the United States is superior to that of the E.U.-15, and, even less, that this nonexistent superiority of the United States was a consequence of a major deregulation of its labor market or of its limited welfare state.

Which Is Richer: The United States or the E.U.-15?

If we take income per capita (measured at market prices) as an indicator of wealth, then several European countries are, in fact, richer than the United States. For the year 2002, the United States had a median income of $36,102 per capita, a lower figure than Switzerland, $52,624; Japan, $50,611; Norway, $45,177; Denmark, $44,740; Austria, $38,477; Sweden, $37,870; Germany, $37,150; and Finland, $36,659. All these countries but Japan are European, and many of them have been governed by social democratic parties either alone or in alliance with other political traditions (other than the liberal, which in Europe is a minority political tradition). If, however, rather than using currencies at the market value we use purchasing-power-parity exchange rates (where currencies are standardized so as to compare the ability to purchase goods and services in the market within each country), then the United States is the richest country. But this indicator is potentially misleading, because it is constructed based on a set of assumptions that favor the private sector of the economy. Purchasing-power-parity exchange rates do not adequately account, for example, for services such as education, health care, home care services, social services, public housing,

and many other public services that are largely excluded from the market in many E.U. countries. If those products and services were included, then the GDP (gross domestic product) per capita would likely be higher in Europe, because those services are much more expensive in the United States than in the European Union.

Which Is More Productive: The United States or the E.U.-15?

It is usually assumed that the greater richness of the United States (which, as we have just said, is questionable) is due to its greater level of productivity—the value of the goods and services produced in an hour of work—compared with that of the E.U.-15 (which is claimed to be about 30 percent lower). It is also widely argued that the rate of productivity growth in the E.U.-15 is lower than in the United States.

When we compare the levels of productivity of the United States with the productivity of several countries of the E.U.-15, we can see that, as described by Mishel, Bernstein, and Allegretto (2), several E.U. countries have higher productivity levels than the United States. If we assign the level of U.S. productivity in 2002 a value of 100, then Western Germany would have had a value of 101; Ireland, 103; France, 103; Italy, 105; Netherlands, 106; and Belgium, 111—all of them, incidentally, with more regulated labor markets and higher public social expenditures than the United States.

As to the rate of productivity growth, Morley, Ward, and Watt (3) have shown that, for the period 1986–2003, the E.U.-15 (as an aggregate) had a growth rate of 1.7 percent, larger than the U.S. rate of 1.4 percent. These authors also indicated that since 1994, the U.S. rate of productivity growth has been higher (1.8 percent) than the E.U.-15 rate (1.6 percent), but when Italy (which had a very low rate of productivity growth) is excluded from the E.U.-15, then the rate is very similar on both continents.

Where Do People Work More: The United States or the E.U.-15?

Another variable that is considered important to explain the income level of a country is the number of hours worked each week and the number of weeks worked per worker each year. The working time per worker is much larger in the United States than in the E.U.-15, a situation that should not be evaluated negatively for the E.U.-15, since this factor helps to explain the higher level of health and quality of life in the E.U.-15 than in the United States. The average vacation time per year in the United States is only two weeks, while it is six weeks in the E.U.-15.

Participation of the Adult Population in the Labor Market

Another factor that helps to explain why the income level per capita is higher in the United States than in the E.U.-15 is the fact that a larger percentage of the adult population works in the United States (71.2 percent) compared with the E.U.-15 (64.8 percent), which is primarily the consequence of a larger percentage of working women in the United States (65.7 percent) than in the E.U.-15 (56.1 percent). If we compare the United States not with the E.U.-15 but with specific countries of the E.U.-15, however, such as the Scandinavian countries (of a social democratic tradition), we find that the percentage of women working is actually higher in these countries (Denmark, 75.1 percent, and Sweden, 73.6 percent, for example) than in the United States.

Other Variables

The *unemployment* rate in 2002 was lower in Ireland (4.3 percent), the Netherlands (2.7 percent), Norway (3.9 percent), Sweden (4.9 percent), Switzerland (3.2 percent), Portugal (5.1 percent), Denmark (4.6 percent), Austria (4.3 percent), and Great Britain (5.1 percent) than in the United States (5.8 percent). For more information on this subject, see the volume edited by David Howell (4), which analyzes the different experiences the OECD countries have had with unemployment and questions the utility of labor market deregulation as a strategy for lowering unemployment. The *annual rate of job production* during the 1995–2002 period was only slightly superior in the United States (1.4 percent) to that in the E.U.-15 (1.2 percent), but inferior, remarkably, to that in France (1.5 percent), among other countries.

Wage differentials, the difference between well-paid workers (the 90th percentile wage earner) and poorly paid workers (the 10th percentile worker), are much larger in the United States—4.8 times for men and 4.6 for women—than in the majority of countries of the E.U.-15. In Sweden the differential is 2.3 and 1.9, respectively. Moreover, wage differentials have been increasing in the United States due to the lowering of wages for the worst-paying jobs, in contrast to many countries in the E.U.-15, where wage differentials have been constant and even declining as a consequence of rising real wages across the full wage distribution. It is also worth noting that all E.U. countries with higher labor productivity levels than the United States have lower wage differentials than the United States.

The *household income* differentials of the United States (using the same difference between the 90th and 10th percentiles of the income distribution) are the highest in the OECD, with a ratio of 5.5. As with wages, all countries in Europe that have higher productivity than the United States still manage to maintain lower household income differentials, calling into question the efficiency–equity trade-off.

The *poverty level* is much higher in the United States than in any European country. Using international definitions, based on relative poverty rates, about 17 percent of the U.S. population (21 percent of children, 24.7 percent of the elderly) lives in poverty, compared with 6.5 percent of the adult Swedish population (only 4.2 percent of children and 7.7 percent of the elderly), 6.4 percent (3.4 percent and 11.9 percent) in Norway, and 5.4 percent (2.8 percent and 8.5 percent) in Finland, and so on, in a large list of other countries.

Given these data, it is surprising that the deregulation of U.S. labor markets and the limited development of its welfare state are presented as a model for the European Union. The economic efficiency of the United States is actually less than that of the E.U.-15. What would the economic efficiency of the United States be if it were subject to the institutional constraints of the E.U.-15 (i.e., the budget deficit limitations, the high interest rates of the European Central Bank, and the miniscule E.U. budget)?

The data presented so far do not demonstrate that the U.S. economy is more efficient than the E.U.-15. Indeed, these data show that, in many respects, the E.U.-15 has been as efficient as the United States, if not more so—a comparison that is even more favorable to the E.U.-15 when the United States is compared with specific members of the E.U.-15, all of them with more regulated labor markets and larger welfare states than the United States. *In the light of this information, it is a profound error for E.U. governments to follow liberal solutions (deregulation of labor markets and reduction of welfare states), because these not only would reduce the quality of life of their populations but also are likely to reduce the efficiency of their economies in important dimensions.*

II. THE LIMITATIONS OF THE EUROPEAN UNION: WHAT ARE THE PROBLEMS IN THE E.U.-15?

The Liberal Dimensions of Some of the Institutional Framework of the E.U.-15

Recently, the rate of economic growth in the aggregate of the E.U.-15 has been below that of the United States—about 1.3 percent in the last nine months of 2003 and the first four months of 2004 in the European Union, for example, compared with 4.8 percent for the same period in the United States. Within the E.U.-15, the rate in Great Britain was 3.7 percent; Germany, 1.5 percent; France, 1.7 percent; and Italy, 0.8 percent. This slower economic growth of the E.U.-15 than the United States is due to several factors. One is that the interest rates defined by the European Central Bank (ECB) have been historically higher and have been declining more slowly than interest rates in the United States, even though inflation has been practically the same on both sides of the Atlantic. Actually, there is no evidence of inflation pressure in Europe, which is a result of the very weak internal demand that characterizes the economic situation in the E.U.-15.

There is almost a consensus that the reason for interest rates being higher in the E.U.-15 (until very recently) and declining much more slowly than in the United States is not a higher risk of future inflation in the European Union. Why, then, this higher interest rate in the European Union? *The answer is a political one:* it is the enormous power of financial capital in Europe, also responsible for the Stability Pact (also referred to, paradoxically, as the Growth Pact), a pact that has created a lot of stability, but very little growth. The Stability Pact limits central governments' budget deficits to 3 percent of GNP, an amount that, under current recession conditions, is insufficient to stimulate internal demand and economic growth. Moreover, this high interest is contributing to a strengthening of the euro versus the dollar. In that respect, it is surprising that liberal authors take the deregulation of U.S. labor markets as the model to follow without taking other characteristics of the "U.S. model" as points of reference. One such characteristic is the behavior of the Federal Reserve Board and of the federal government (they have tolerated deficits of 5.4 percent of GNP). Contrary to what is believed in liberal circles, the Federal Reserve Board is highly centralized and, at least in theory, cannot ignore the political positions of the U.S. Congress. The ECB, however, is insensitive to the opinion of the E.U. Parliament, with a degree of independence that does not exist in the U.S. Federal Reserve Board (or any other central bank in any major country). The ECB has a highly decentralized structure, with the directors of the central banks of the E.U. member states holding great power. The meetings of the ECB Board of Directors are secret, and there are no public minutes of these meetings. There is not even a semblance of public accountability. The Federal Reserve Board, on the contrary, publishes minutes of its meetings, and its director meets regularly with the U.S. Congress. The minutes are publicly available, and the public can learn which decisions are taken and the rationale for taking them. Not so in the European Central Bank, where control by the banking community of the ECB is almost absolute. It is because of this situation that the primary mandate of the ECB is the control of inflation (and only theoretically the stimulation of economic growth).

This responsibility and governance is clearly spelled out in the E.U. Constitution and is one of the major reasons for the slow economic growth in the E.U.-15. What is happening now in Europe is very similar to what happened in Spain in the 1980s. At that time, the high unemployment in that country was attributed to the rigidity of the labor market and to the "excessive generosity of the Spanish welfare state," as the director of the Spanish Central Bank, Mr. Rojo, once complained. (Spain has one of the lowest percentages of GNP in public social expenditures in the E.U.-15.) The actual cause of the high unemployment, however, was the very high interest rates (the highest in Europe) that made it very costly for business to invest and for consumers to consume. We are seeing the same process now in the European Union. As in Spain in the 1980s, banking in Europe is enjoying some of the highest profits of the past 30 years (see 5). Meanwhile, some of the business associations (and very much in particular,

mid-sized and small business associations, such as the EUAPME, the representative body of Europe's Small and Middle Size Enterprises) are protesting the ECB policies.

A significant decline of interest rates is indeed a requirement to stimulate economic growth. The reduction of interest rates, per se, is insufficient, however, unless there is an expansion of consumption and investment, stimulated by a considerable growth of public expenditures, allowing for larger public deficits. Part of those public expenditures should be invested in facilitating the integration of women and young people into the labor force. Such integration requires major investments in the development of networks of services, such as childcare centers, home care services, housing, and others that facilitate such integration. In that respect, it is a mistake to try to stimulate internal demand by tax cuts, which tend to be highly regressive and have a very limited effect in stimulating the economy. Public expenditures, particularly public social expenditures, have much more effect in stimulating the economy than do tax cuts. Public expenditures tend to benefit the popular classes, which are the ones with a higher propensity to consume. Another major obstacle for stimulating economic growth in the European Union is the lack of coordinated economic and fiscal policies as well as the very limited resources that exist for redistributional purposes. As we mentioned before, the budget available to the European Commission represents only 1.27 percent of GNP, much smaller than the U.S. federal budget, which is 19 percent of GNP. It is very difficult to correct regional differentials under these conditions. It is worth clarifying here that when the Economic and Monetary Union was first established in the 1970s, some of its original proponents (such as the Chief Advisor to the U.K. Treasury, Sir Donald MacDougall) thought the E.U. budget should be 5 to 7 percent of the combined European GNP, if it was to be used as an instrument in influencing the business cycle. This figure was not accepted. The current figure of 1.27 percent was fixed at the Berlin Summit of 1999 for the period 2000–2006.

Is the Welfare State in Europe Sustainable?

Another position widely promoted by liberal authors (and by the European Central Bank) is that, due to the aging of the E.U. population, the welfare state in Europe is not sustainable without dramatic and substantial cuts in social benefits. An article in the fall 2004 bulletin of the ECB indicated that health services can no longer be sustained as universal (i.e., distributed to all citizens and residents as a matter of right), and rather must become an assistential program (i.e., a means-tested type of program). A less dramatic proposal is the one put forward by some political leaders, even some within the social democratic tradition, of reducing social benefits, with a guarantee, however, of a minimum benefit for everyone. That minimum would be complemented with privately funded provisions of services and benefits. There is active pressure to privatize social transfers

and public services, reducing the size of the public's responsibility for maintaining the social well-being of the population.

The theoretical justification for the majority of these positions is the demographic transition that is taking place in the E.U.-15, an outcome of the lowering of fertility rates and the lengthening of life expectancy. It is assumed that demographic transition means a lowering of the number of contributors to the social security trust funds (most concerns about the sustainability of the welfare state focus on pensions and health care) and an extension of the number of years that the elderly enjoy the social benefits.

These arguments are important ones. And they seem to be plausible. Indeed, the growth of the percentage of elderly in the whole population plus the increasing number of years that elderly people live translates to a substantial growth in pension expenditure, as well as health and social expenditures (such as home care services, convalescent homes, homes for the elderly, and others), since the elderly are the people who use health and social services most extensively.

Before reaching these catastrophic conclusions, however, we need to consider several factors. One is that the sustainability of public social programs depends not only on the extension of public social expenditures, but also on the amount of public resources available. This amount depends on, among other factors, the rate of economic growth, the rate of productivity growth, and the percentage of the population that works. If, for example, the percentage of women working in Spain were the same as in Sweden, the sustainability of pensions would be guaranteed in Spain until 2050. Also, a growth in productivity would enable the state to receive higher contributions without reducing the standard of living of the taxpayer. Let's assume, for example, that today we have three workers (the majority of taxpayers are salaried people) earning 1,000 euros per week. Together they earn 3,000 euros. If each worker pays 167 euros to sustain a pensioner (who receives 500 euros), he or she keeps 833 (1,000 – 167) euros. In 2040, if the growth of productivity of each worker in the coming 40 years remained the same as during the last 50 years (a conservative estimate, since it is likely that productivity will grow more rapidly), then each worker should produce double that amount—that is, 2,000 euros. In that case, it would require only two workers to produce 4,000 euros, a larger amount than that produced today by the three workers. If the pensioner were to receive, in 2040, a pension that is double what a pensioner now receives, he or she would be getting 1,000 euros per week; this would derive from 500 euros per contributor, who thus would retain 1,500 (2,000 – 500) euros each, much larger than the amount a contributor retains today. Due to the growth of productivity, both the worker-contributors and the pensioners can have increased incomes (in this estimate, the impact of inflation has been taken into account by using euros with the same purchasing power). Thus, it is important to stress that most catastrophic predictions of the unsustainability of the welfare state are based on exaggerated rates of decline in the growth of the economy and productivity.

Another argument that is usually put forward for the unsustainability of the welfare state is that the growth in numbers of the elderly increases the ratio of dependency (i.e., the number of beneficiaries per contributor). Thus, it has been estimated that this ratio would increase in Europe over the coming 25 years by 40 percent. If, however, we add in children as dependents, then we can see that, due to the reduction in the percentage of children in the population, the ratio of *total* dependency (elderly plus children) will increase only 10 percent during the coming 25 years, since the growth in numbers of elderly will be compensated for by the decline in numbers of children.

On the other hand, Francis Castles (6) has shown that during the past 30 years, there has not been a statistically significant relationship between aging and growth of public social expenditures. The European countries that have seen a larger growth in public social expenditures (Switzerland, Sweden, Norway, and Denmark) have not experienced a specifically higher growth of the elderly in their populations (except Sweden). And, vice versa, Spain, Greece, and Italy *have* seen a large growth of the elderly in the population (the elderly being a higher proportion of their populations than the OECD average) without a large growth of public social expenditures (lower than the OECD average).

As these data show, there is not a universal tendency toward larger public social expenditures as a result of the growth of the elderly population. Indeed, between aging and public social expenditures, there is a whole set of political, cultural, and institutional variables that preempts the possibility of establishing a direct relationship between aging and public social expenditures. It cannot be said that one will determine the other. It depends on a whole set of variables that dilute the impact of one on the other, bringing into question the idea that the growth of aging means a crisis of pensions or of the welfare state. Actually, the sustainability of the pension system depends much more on the intensity and levels of coverage of these benefits (political variables) than on demographic variables. There is not, therefore, a demographic determinism that leads unavoidably to the crisis of the public pension system or of the welfare state. The large variability in the pattern of public social expenditures is explained much more by political than by demographic considerations, as a consequence of the ability of each state to respond to each specific situation. This variability of public social expenditures also brings into question the theories about the convergence of public social policies in Europe due to demographic transitions.

Finally, one last factor that has been presented as determined by changes in demographics is the need to rely on the immigrant population as a way of resolving the problem created by a diminishing fertility rate. Frequently, immigration is presented as the solution to the problem of the E.U. pension system. Putting aside that there is no pension problem, such an argument ignores the fact that the impact of immigration on the fertility rate will be a

rather short one, since immigrants' fertility rates soon adapt to those of their adopted country. But more importantly, this argument ignores the political nature of the problem. The rate of immigration in a country is also a political variable. Southern E.U. countries (such as Spain) with a very low participation of women in the labor force have chosen to resolve the shortage of labor by relying on immigration rather than by encouraging women to enter the labor market. Spain (where the Chamber of Commerce calls for 100,000 immigrants per year) would have 6 million more workers (and taxpayers) if its rate of women's employment were similar to Sweden's. Spain's choice of immigration rather than women's integration is the result of class power relations (unions are very weak in Spain) and gender power relations (sexism is still very powerful in Spain). The reverse occurs in Northern Europe, where fertility rates, incidentally, are much higher than in Spain.

The social investments, such as the previously cited networks of family supportive services that are aimed at integrating women into the labor force, are very important to guarantee the sustainability of the welfare state. The fertility rate in an E.U. country depends on the availability of these services as well as on a labor market that allows women to gain their autonomy and independence, enabling them to combine their personal professional projects with their family commitments and responsibilities. In that respect, the Northern European countries have been successful in reversing their declining rates of fertility by providing the supportive family conditions that can resolve this situation.

Conclusion

In this section we have shown that the liberal policies now being advocated (which include deregulation of the labor market and reduction of social benefits), even by social democratic governments in Europe, are economically and socially inefficient. Moreover, the liberal elements built into the framework of the E.U. institutions (and reflected in some articles of the E.U. Constitution and in the Nice Treaty) are responsible for the slowing of economic growth and for the high unemployment that have recently characterized the E.U.-15—a situation that explains the growing disenchantment with the European project of large sectors of the population, and especially the popular classes that are most negatively affected by these liberal policies. The alternative is to change some elements of the framework to incorporate elements that have proven successful in other settings, including in the United States (a dimension of the "Anglo-Saxon liberal model" that is ignored by liberal thought)—that is, lower interest rates, more public accountability of the European Central Bank, and the development of a federal structure, with larger resources available to the E.U. government for distributional purposes and with a higher level of democratic participation and economic and fiscal coordination.

III. WHAT CAN BE DONE TO MAINTAIN AND EXPAND THE SOCIAL MODEL IN EUROPE?[2]

A Brief Historical Review: Where We Are Coming From

As the previous sections have shown, the establishment of the social model in Europe—one of the most important developments in the 20th century—was both the cause and the consequence of a very efficient economy, which was in many important dimensions more successful (and continues to be so in many economic areas) than the liberal model in existence in the United States. The European social model was based on full-employment policies predicated on a social pact between labor and capital, led by the two major political traditions in existence in Europe: the social democratic and the Christian democratic (or conservative, based on Judeo-Christian values) traditions. Needless to say, that economic growth was greatly assisted at the beginning of the post World War II period by the Marshall Plan, funded by the United States. The primary stimulus for the growth, however, was the enormous increase in the public sector, which increased its share of GNP by 10 percentage points in just ten years between 1950 and 1960 (from 30 to 40 percent) (7).

This economic growth was rooted also in the economic stability provided by the currency exchange program based on the U.S. dollar. The growth of Europe (and Japan) led to a multipolar world capitalist economy in which the strength of the dollar weakened the competitiveness of the U.S. economy. This situation led to the deliberate collapse of the Bretton Woods agreement, allowing first for a realignment of exchange rates with respect to the U.S. dollar in 1971 and later, in 1973, a complete floating of the exchange rate system. This explains why Helmut Schmidt, chancellor of West Germany, and Giscard d'Estaing, French president, established the European Monetary System in 1979, an exchange rate mechanism among the European currencies and the first step toward a single European currency, the euro. A lesser cited cause for the establishment of monetary stability in Europe was the growing labor unrest, a result of seemingly unstoppable inflation. This unrest stimulated the radicalization of labor relations and the strengthening of the conservative response, which led in the United States to the election of President Carter (the most conservative Democratic Party president the United States has had) and later President Reagan, and in the United Kingdom to the defeat of Callaghan (due to the "winter of discontent") and the victory of Thatcher. Let's not forget that, in 1979, Paul Volcker, governor of the Federal Reserve Board, engineered a dramatic increase of interest rates that created a worldwide recession. This policy also had the intention of creating high

[2] This section is influenced by George Irvin (7) and by a discussion at the CIDEL Workshop "Which Social and Tax Policy for Which European Union?" that took place in Stockholm, June 10–11, 2005, at which a draft of this paper was presented.

unemployment rates as a way to discipline labor. It was the beginning of the substitution of Keynesianism with monetarism and supply-side economics, which depend on the elimination of demand management and its replacement by what Susan George has called the 3D's: *deregulation, devaluation,* and *deflation.* The International Monetary Fund (IMF), whose credits were called upon then more than ever (due to the worldwide recession), became a major worldwide promoter of neoliberalism. The bases for the *Washington consensus* were established at that time, the end of the 1970s and beginning of the 1980s.

The Brussels Consensus

The European translation of the Washington consensus was the *Brussels consensus,* which appeared in the 1980s, along with the Maastricht economic rules, when inflation was very high in Europe and public debt was growing very rapidly in many countries. In Belgium, Greece, Italy, and Ireland, public debt exceeded 100 percent of GDP, and public deficits were close to 10 percent of GDP. Germany and the northern European countries were afraid of the recklessness of the southern European countries. These fears explain the attractiveness of monetarism to the architects of the Maastricht Treaty. Moreover, the Mitterrand failure to stimulate the French economy by stimulating Keynesian public policies (with the subsequent decline of the French currency, vulnerable to the financial market's speculative pressures) further strengthened the attraction of monetarism and supply-side economics. And at the time the Maastricht Treaty was signed in 1992, many of the European currencies (Italian lira, French franc, British sterling, and others) were in trouble. The attractiveness of the *Washington consensus* in Europe was thus very powerful. The Maastricht criteria, with their primary objective to reduce inflation (no higher than 2 percent on average) and calling for a balanced budget for the entire economic cycle (no more than 3 percent of public deficit) and a public debt of no more than 60 percent of GDP, were thus established. These policies were highly successful in reducing inflation and in establishing a certain monetary stability in Europe, even though individual currencies would still be subject to speculative attacks by the ubiquitous financial markets.

That limitation of inflation had a cost, however: slower economic growth, higher unemployment, and slower growth of public expenditures, including public social expenditures, in the 1980s and 1990s than in the previous period of the 1950s to 1980s. In 1999, the euro was established. The supposed wisdom of *monetarism* was also apparently demonstrated in the United States when elimination of the federal deficit by Clinton was wrongly presented as the cause for the substantial growth of the U.S. economy in the 1990s. Actually, U.S. economic growth after elimination of the federal deficit was remarkably slow, and only after 1995 did it grow significantly as a result of stock market speculation centered around technology stocks (the famous Wall Street bubble).

The euro has indeed been a success in providing monetary stability. But its greatest success has been to make that currency (like the U.S. dollar) more resistant to financial market speculators. Because of its size (like the dollar and the yen), the euro is difficult for speculators to attack, and the ECB could respond fairly easily to these kinds of activities. This means that, once the euro had taken root, successful *Keynesian policies could indeed be implemented.* As was seen in the United States under Reagan and Bush (and in Japan), large deficits—well beyond the limits set by the SGP (see below)—could be carried without accelerating inflation or speculative attacks.

Moreover, as George Irvin (7) has highlighted, the Maastricht criteria of the Stability and Growth Pact (SGP) have major problems, which include: (*a*) an excessively low inflation rate as an objective, which interferes with economic efficiency; (*b*) the arbitrary nature of its fiscal indicators (why a 3 percent deficit ceiling and not 5 percent, for example?); (*c*) fiscal limits that are no longer necessary now the euro has been established; (*d*) a lack of sensitivity about the different types of deficits (current vs. capital public expenditures); and (*e*) the deflationary impact of the requirement to achieve balanced budgets over the economic cycle, which can require surpluses of up to 3 percent of GNP in good times to compensate for deficits of up to 3 percent in bad times.

Where Was the Social Dimension of the Maastricht Treaty?

It would be unfair, however, to see the *Brussels consensus* as a mere reproduction of the *Washington consensus.* Indeed, parallel to the monetary policies outlined above, there was a series of proposals that were presented as "socially friendly." The Delors White Paper even warned against "wholesale labor market regulations," and the Lisbon European Council in 2000 introduced the concept of social expenditures as investment rather than consumption (8). Moreover, under the leadership of France and Sweden, the E.U. Council documents spoke about the need for full employment. But these social concerns and dimensions were never fully developed and were never allowed to contradict the monetary policies that characterized the *Brussels consensus.* Actually, even in comparative terms, the *Brussels consensus* was much less socially concerned than the earlier Paris consensus, appearing in the Treaty of Paris of 1951, which established the European Coal and Steel Community (ECSC), the precursor of the European Union. In that treaty, the top authority of the ECSC had the power to penalize firms that used low-paid workers to undercut competitors. Later, the Treaty of Rome of 1957 encouraged the establishment of a central coordinating agency responsible for promoting the development of employment law, social security, vocational training, and occupational health, with a mandate to harmonize these conditions.

The process that started with Maastricht, however, evolved to become much less socially concerned, leading to the situation of social insensitivity that appears

in the Bolkestein directive, the draft of which (in 2004) was prepared under the auspices of the European Commission presided over by Prodi (paradoxically, the candidate of the social democratic parties). Such directives allowed services provided in other E.U. countries to abide by the laws of the countries "of origin," which basically meant that plumbers from Poland, for example, could work in Germany and get paid according to Polish wages and Polish regulations. This directive was a frontal attack on labor in the E.U.-15 countries. Resistance to the directive led to the modification that workers from new E.U. countries, when foreign workers in other E.U. countries, would be paid at least the minimum wage of the recipient country, thus establishing two levels of salaries for each occupational sector: a minimum wage for immigrant workers and a labor market wage for local workers. This arrogance of capital and clearly aggressive anti-labor intervention was one of the mobilizing forces for the *no* vote against the European Constitution in France and the Netherlands and the growing unpopularity of the European Union among the European working classes.

Actually, the Bolkestein directive is just the extreme form of a normal situation in which European labor has been weakened considerably. There is, for example, no legislative space in the European Union to allow for a European collective bargaining agreement. Although monetary policy is centralized, economic fiscal, social, and labor policies are decentralized to the national levels, weakening labor significantly. This means that, at the E.U. level, workers can defend themselves individually (against discrimination) but not collectively. As Bercusson (9) has indicated, labor law in the European Union resembles labor law in the United States, whereby the absence of federal legislation on collective bargaining means that the only way that workers can protect themselves is through anti-discriminatory federal legislation—which explains the enormous development of anti-discriminatory legislation in the United States. Needless to say, this situation favors employers and disfavors labor.

The Need for Change

These limitations explain the need for a substantial change in the framework of the European Union, in the directions outlined in Section II. There is a need for *more* Europe to save Europe. The state of the current Europe, a result of the excessive power of financial capital and, to a lesser degree, corporate business interests at the cost of labor, explains the growing unpopularity of Europe among the working classes, who saw Europe as the social Europe they had fought for and had hopes for. The limited development of the social dimension of the European Union results from its very restrictive democracy.

The orientation of the needed change should be clear. The centralized nature of monetary policy has to be accompanied by centralized economic, fiscal, social, and labor policies to dilute the excessive power of monetarist interests. Then there is a need to dramatically change the SGP by eliminating it. It should be

replaced with a new coordinating committee that goes much further than the current Broad Economic Policy Guidelines. A European Stabilization Fund (ESF) could be administered by the European Investment Fund (EIF), with each member state developing plans for responding to recessions and overheating, and the possibility for the fund to respond to excessive contraction or expansion (more than 2 percent of GNP) (10, 11). The activation of the ESF could be approved by the Council for Economic and Financial Affairs (ECOFIN), and its principles by the European Parliament. The ESF would also promote long-term investments at the E.U. level.

Another possible intervention could be the establishment of a federal E.U. budget of 5 to 7 percent of the European GDP, an amount large enough to be used as an instrument to regulate the European economic cycle. This budget should be funded only partly by a value-added tax (which is regressive) but also by progressive taxation by the states. Also, some form of tax coordination (although not harmonization) should be developed.

These fiscal and economic policies should be complemented by the development of common welfare state policies to guarantee social rights, established in a new constitution and developed operationally under the guidance of criteria developed by the European Parliament, and developed in such a way that no country will see a reduction in its welfare benefits. Only under these conditions can the European project become attractive to European populations—and in particular to the popular classes that have been directly threatened by the monetary and fiscal policies that have been the product of the *Brussels consensus.*

Note — This article is adapted from a paper presented at the CIDEL Workshop "Which Social and Tax Policy for Which European Union?" held in Stockholm, Sweden, June 10–11, 2005.

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