



European Ideas Network

Think Tank Cooperation 2006

TF 2 European Social Models and Economic Reform

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Abstract

Analysis

1. An important contribution to stable economic development is the European economic and social model. Social models or social security systems have a value that go beyond the management of poverty, illness and need. They contribute to a general social peace. But they are not limited to this. They support economic stability and the competitiveness of economies, locations, businesses and employees.

2. Yet, because every Member State follows an adapted policy of social equity (the leveling of income or social differences is a central difference between the socialist vision and the EPP concepts) in accordance with its own historical development, no single, uniform European social model exists at present.

3. A trade-off between economic growth and social policy measures is not mandatory. Economic performance is a precondition for a generous social policy. The question whether Europe's ability to compete and correspondingly its Member States suffer under the European social model has no standard answer. If the respective social model operates, in the best sense, in a market-integrated and preventative manner, then it will sustain the competitiveness of the national economy. If, however, the social model leads to the exclusion of a significant portion of the population from the markets or functions more like a reactive repairman of market events, then it decreases the competitive ability of that particular state.

4. Looking at the different social models we can observe a convergence of policies – at least a limited convergence. Expenditures in different social security systems have been curbed or the aim to do so was voiced and there is a shift away from financing social security systems via contributions by employers towards financing via taxes.

Conclusions

1. A *uniform* European social model is neither possible nor desirable. The “social laboratory” of Europe is an important element in ascertaining the advantages and disadvantages of national social arrangements and in carrying out benchmark comparisons. Competition helps nations to “strive for excellence” and learn from each other. All European social models have a future, none are doomed per se.

2. Common principles and characteristics of the European social model can be found in all Member States and they can be part of a kind of “*European Social Agenda*”. Next to philosophical foundations they include the notions that free competition requires a well-regulated system and that state institutions provide a (differing) degree of social security. Upon the requests of its citizens, the social model must be prepared to make the required adjustments, protect citizens from insecurity and uncertainties, strengthen the readiness for change, and encourage self-confidence in the future. A corresponding social policy requires courage on the part of the respective societal actors, governments and political leaders.

3. Common criteria for the success of a social model are: efficiency, effectiveness, equity (in the sense of social justice), and sustainability – these are the requirements which a European social agenda must satisfy. In doing so, some Member States are achieving better results than others. From this, it is essential to learn. Successful countries and country groups (above all the north European and the Anglo-Saxon countries, but also the Netherlands and Austria) place emphasis on an “investive/investing” social security. To this belongs above all an active labor market with

high labor participation (precisely from labor market problem groups) and tending towards low labor market regulation -- despite often having strongly divergent social levels. The need for adjustment is at present greatest in the Continental European and Southern European Member States.

4. The perpetual modernization of Member State social models remains of vital importance for the economic success and the acceptance of the EU – also in today’s successful countries: not only so that all Member States can perform their own economic contribution for a future of Europeans, but also so that Europe can preserve its fundamental social values and remain a credible contender for economic and social advancement throughout the world.

5. Change is inevitable given the major shift in demography and ageing. Change and competition drive economic wealth. The European social model can contribute to more acceptance of change. In so doing, however, a lengthy debate over which type and degree of social security will enable Europe to meet the economic challenges of the future will have to take place.

Recommendations

1. Values and principles

European Economic and Social Models are based on common philosophical values: the undeniable dignity of mankind: liberty, compassion, rights and responsibilities and subsidiarity.

2. Goals

Employment is the core of a healthy European economical and social model. 20 million jobless and more than 80 millions inactive people in the European Union represent the mayor problem of economic reform and social stability.

The Social Model is not an end in itself. It has to underline, not undermine the values of Europe. It has to contribute to economic strength, competitiveness and labor market participation.

3. Measures

Strengthen overall employment rates and the role of labor market participation

Respect different roles of state and government

Complete the Single Market

Aim for sound money and sound finance

4. Messages

- Social Protection is not a lifestyle; it is an opportunity for a second chance!
- Make work pay!
- Only work pays!
- Less protection, more enabling!

1 Foreword

The countries of the European Union have reached high levels of prosperity, social cohesion, environmental protection and quality of living. More than 300 million citizens are part of a common market and share a common set of values.

Yet at the same time, Europe and its Member States are faced with great challenges. Globalization enables the exchange of goods and services or the possibility of work throughout the world. With this, economic development, higher living standards and improved social protection against risks of life continue to grow. Well-regulated competition will not only become a source of economic prosperity, but also of social progress. With this unique, one-time mixture of economic strengths, stable relationships and life opportunities for broad levels of the population, Europe has the opportunity to promote its approach worldwide.

A common European social model is not however an end in itself. It must contribute to Europe's competitive position, its Member States and citizens. The question whether this can be managed, finds varying degrees of encouragement and criticism in all European Member States.

On the one hand there is the sense that because of its high costs, state-sponsored social security endangers European companies' competitiveness, and because of its ample social safeguarding of the unemployed, it weakens motivation for returning to work. In addition, strong regulation of the labor and product markets limits mobility and the dynamics of innovation as well as contributing to European mass unemployment, which is presently higher than in Japan or the USA.

On the other hand, the European social model is still at its core sustainable. A strong, universal and public social security, good health insurance, high pensioner levels, a modern, public infrastructure connected to highly qualified employees is perceived as necessary in order to ensure Europe's sustained economic growth, competitive ability and attractiveness for investors and highly skilled workforce.

With the Eastern enlargement, Europe is growing together both economically and politically with breathtaking dynamic. With it though, views on a common European social model have become even more diverse. The new Member States have understood their entries as a major opportunity for prosperity and development. Still, it should be acknowledged that they are weary of overstressing social protection and the loss of their comparative advantages. This will affect their attitude towards further development of European social security.

Thus it is all the more important to develop clear and common conceptions of a European social agenda. That such is still lacking is evident in the citizens' rejection of the European Constitution. Yet, the people of Europe did not reject per se the change and personal adjustment necessary to the challenges of globalization. Rather, they refused the uncertainty over the chances of their own personal development and over the security of their therewith bound personal risks. Abolishing these uncertainties and creating the groundwork for change to be understood as a chance for greater prosperity and a better life is the responsibility of politicians and policy.

The flexibility and risk readiness of Europeans and the European Member States will improve in accordance with the degree to which the European Union succeeds in recreating a solid groundwork of inner conviction of its values and principles. The European social model can make an important contribution to this effort.

This paper addresses the contribution of the European social model to the competitive ability of Europe:

- Which principles unite the European perspective on social models?
- Which of the various features of social models allow single Member States to handle the challenges of globalization with more ease? Which make it more difficult?
- In which way can the European social model be developed further so that Europe's competitiveness, its citizens, enterprises and institutions are strengthened?

It is an illusion to believe that Europe and its common social model is an "island of the blessed", afforded the opportunity to observe globalization from afar, arbitrarily adapting to and absconding from the necessary adjustments.

2 The European Social Model: common principles – diverse characteristics

The predominant view among Europeans is that there is no single, uniform social model utilized similarly by all Member States. In addition, jurisdiction on questions of social policy is also lacking on the European level. However, the diverse features of the European social model can be traced back to common principles.

2.1 Common Philosophical Foundation

1. In the heart of the matter is the human being with its undeniable dignity and liberty. According to this principle of dignity of the individual (personality) every human being has the right and obligation to use his freedom to develop his abilities. He is self-responsible for his life and the use of his freedom. Every human being has the right to participate fully in the civil society and its activities: culturally, economically etc. Discrimination has no place in this approach.
2. Society accepts solidarity in a sense of compassion for those in need. This is however a twofold obligation, no “one-way-street”: the individual vis-à-vis the society and vice versa. Rights and responsibilities are constitutional for this approach– individual discipline against the misuse of facilities for the most. Where public institutions guarantee a social minimum standard of living, the needy have to do whatever he can to get out of transfers and supportive structures and offer any abilities to the society.
3. The principle of subsidiarity structures the responsibilities within society: first of all and above all, the individual is responsible for himself. Where his abilities are not sufficient for him to sustain himself, family responsibility sets in. It passes on to the community and to the next institutions – only at the end of the range there is the state with its public institutions. When capacities are sufficient for the individual, they have to contribute to the wealth of the common good (society).
4. These principles are somehow universal. They expand beyond the EU-borders. There is a responsibility of the EU to develop an international legal framework for a globalized world, for global competition and for Less Develop Countries and their possibility to participate in the international division of labor.
5. To provide sustainable structures for next generations is just as important in environmental questions as it is in public budgets.

These seem to be common philosophical foundations that together with the following common principles could formulate a “European Social Agenda”.

2.2 Common Principles

Characteristic to all European social models is an active and determinant role of the (social) state as an actor in economic development. It is viewed as the backbone of society. The citizens are ready to recognize the role of the state and are prepared to provide the financial means for it. A functioning public sector is understood as an (economic) advantage. The public sector operates as a regulator, guarantor, redistributor, and service provider, in particular:

- Regulating markets for the purpose of a controlling competition;
- Facilitating education;
- Offering at least partial collective security for major risks of life (health, old age, unemployment);
- Guaranteeing social consensus as a means of balancing the interests of the employer and employee;
- Providing further public services (existential provisions).

Competitive ability and an increase in prosperity are thus not based exclusively on free, unregulated markets, rather on specified competition and social regulation through the state.

Throughout its creation and use, the European social model has been marked by two major streams of thought with the fundamental concepts being connected with the names Otto von Bismarck and Lord William Beveridge.

At the end of the 19th century, Chancellor Bismarck created the foundation for German social security (state health insurance, accident insurance, the old age pension scheme and later unemployment insurance). Yet, the real innovation came in the introduction of the principle of insurance with a clear connection between contribution and benefits claims. Self-help facilities and centers had only a supplementary function. The income security of the industrial worker against major life hazards was a social political goal, insurance allocation was not based on need, rather on the once achieved salaried income; thus, it was achievement orientated.¹

The convictions of the British economist and social politician Beveridge were of a different nature. His plan aimed at abolishing poverty: every citizen was to receive a sufficient income on which to live. The state was to provide for this form of social security, as it was also responsible for the (taxation) financing it. A direct relationship between contribution and later achievement was unimportant for Beveridge. The degree of state support was attached not to claims of achievement, but rather to needs.

¹ The influence of the Catholic school teachings (having taken up liberal elements) in Germany should not be overshadowed. Their principles of personality, public interest, subsidiarity and solidarity are somehow in conflict with the corporative approach of the Bismarckian welfare state.

2.3 Diverse Characteristics and groups of the European Social Model

In each Member State (MS), the type and degree of the role of the government and the level of social protection is regulated differently. The balance of market (competition) and social regulation follows an own unique way. The different scopes of the public sector can be expressed represented by the following few indicators (among others):

	Total general government revenue % of GDP	Total general government expenditure % of GDP	General government final consumption expenditure % of GDP	Social security transfers % of GDP	Social expenditures (b.) % of GDP	Net saving of general government % of GDP
Austria	49,3	50,6	18,0	19,2 (MAX)	29,1	- 1,3
Belgium	49,3	49,3	22,6	16,0	27,8	0,0
Czech Republic	41,5	44,6	22,9	11,8	19,9	- 3,0
Denmark	58,9 (MAX)	56,3	26,7	16,9	30,0	2,6 (MAX)
Finland	52,5	50,7	22,4	16,8	26,4	1,3
France	49,8	53,4	23,9	17,7	30,6	- 3,6
Germany	43,2	46,8	18,4	19,2 (MAX)	30,5	- 3,6
Greece	46,0	52,0	17,1	18,7	26,6	-6,0 (MIN)
Hungary	44,6	48,9	22,6	14,2	20,9	- 4,3
Ireland	35,6 (MIN)	34,2 (MIN)	16,0 (MIN)	9,2 (MIN)	16,0 (MIN)	1,3
Italy	45,4	48,5	19,2	17,3	26,1	- 3,1
Luxembourg	44,8	45,9	18,2	15,7	22,7	- 1,1
Netherlands	46,2	48,6	25,0	12,3	28,5	- 2,3
Poland	40,2	45,0	17,6	15,3	22,1	- 4,8
Portugal	45,4	48,4	21,4	14,9	25,4	- 3,0
Slovak Republic	45,7	49,0	20,3	10,4	19,2	- 3,3
Spain	38,4	38,6	17,4	11,7	20,2	- 0,3
Sweden	58,3	57,3 (MAX)	27,7 (MAX)	18,0	32,5 (MAX)	1,0
United Kingdom	40,8	43,9	21,2	13,4	27,6	- 3,1

Notes: a. 2003 b. 2002

Source: *National Accounts of OECD Countries*, OECD, Paris, 2005.
StatLink: <http://dx.doi.org/10.1787/444141640346>

The varying features result from the different social systems emerging from and growing in dissimilar historical, political and cultural circumstances.

Esping-Andersen offers a first possibility for the groupings of the welfare state (here as a synonym for social model group), categorizing them into liberal, conservative and social democratic paradigms:

The **liberal** welfare state (Great Britain, present day Ireland, also the USA, Australia, and New Zealand) stresses above all the role of the free market and the family; social entitlement rights are limited and are often linked with individual poverty tests. Social stigma is frequently attached to these. It is predominately financed from the state budget. Intervention in the labor market occurs – when at all – above all to break up incrustations and to ensure freedom of contract. This type strongly emphasizes the aspect of freedom, the values of individual responsibility towards family and society.

The **conservative** welfare state (e.g. France, Italy, Germany, and the Netherlands) intervenes to strengthen the markets, first temporarily and primarily for governmental political reasons. Social protection is based on life long job biographies with social insurance contributions that deliver entitlements (in the sense of property rights). As life long jobs are supposed, job protection is relatively high. This type is shaped by the aspect of corporate solidarity.

The **social democratic** regime (Sweden, Norway and Denmark) are arranged in a universalistic manner; equality in the sense of widespread sharing of wealth is its aim, based on social civil liberties. It is likewise financed through tax revenues/public budget; at the same time public services are on high levels and have key functions in socio-political terms and on the (public) labor market. The trust in the role of the state/government is relatively high.

In turn, *Andre Sapir* recognizes four different groups of European social models. All the models intersect in some manner and all have unique selling points.

Nordic social model

The Nordic social model characterizes the notion of **Flexicurity**. Small labor market regulation is combined with high levels of protection (unemployment benefit). An activating labor market policy encourages the goal of a quick resettlement in the labor market. The confidence in the state as an effective societal and economic political actor is high. Labor relations are especially important and the rate of unionization is phenomenally high.

Anglo-Saxon social model

The Anglo-Saxon model is distinguished by limited market regulation. Social protection is ensured individually through market participation and less through collective security systems. The state sector tends to be smaller. Income disparities are correspondingly more greatly pronounced.

Continental European social model

In the large Continental European countries, a high degree of labor market regulation in combination with strong social protection dominates the system. Even after the latest reforms, the state remains an important actor in economic policy. The collective security of risks of life is guaranteed through a high degree of social transfer. The role of labor relations and of social consensus is great; however, the rate of unionization is declining. Protectionist tendencies are greater in the large countries than in the small countries or in the Anglo-Saxon model. The meaning of individual responsibility is not as clearly stressed, because of a high part of collective security systems.

Some of countries that follow the Continental European model like the Netherlands or Austria differentiate themselves at the moment from countries like Germany, France or Italy as a result of their significantly better economic development.

Mediterranean social model

The Mediterranean model shares similar characteristics with the continental model in its strong labor market regulation. The level of social security, however, is less pronounced and is concentrated above all on pension insurance. High risks of poverty and the unevenness of income distribution resemble the Anglo-Saxon model. The low labor participation rates though are again comparable to the Continental European model.

2.4 Classifications of the four European social models

	Nordic	Anglo-Saxon	Continental	Mediterranean
Principles				

Market Regulation	Low	Low	High	High
Role of the State	High	Low	High	Low
Type of Social Protection	Collective	Individuell	Collective	Individuell
Level of Redistribution	High	Low	High	Low
Performance				
Labor Participation	High	High	Low	Low
Sustainability	High	High	Low	Low
Equity	High	Low	High	Low
Shadow Economy	High	Low	Low	High

2.5 Point to Note: The EU Constitution

Art. I-3 paragraph 3 of the Constitution of the EU, in reference to the goals of the Union, includes a “competitive social market economy”.

The social market economy as the backbone of the German economic miracle under Chancellor Konrad Adenauer and the Minister of Economics, Ludwig Erhard, is a synonym for the economic, social and societal catching up process of the 1950s and 1960s. This model rests on the principles of Catholic social teaching as common philosophical foundations (s.a.).

Ludwig Erhard social market economy, however, should not be confused with Bismarck’s understanding of the social state or the Continental Social Model from nowadays.

The social market economy on the one hand (comparable to the liberal model) stresses individual’s rights and duties and accentuates the power of free markets as the Anglo social model. On the other hand, the powerful results of competition and freedom on market should be (re)distributed in a fair way, that all people should profit from these benefits. In this sense it leans towards the Nordic social model.

Founding fathers of the social market economy regarded the fundamental ideas of the Bismarckian system of strong collective protection with skepticism. Today, a wide variety of German policies (labor market, fiscal policy, education, taxation, federalism) breach the principles of the social market economy. Thus, its current performance also falls behind when compared to the Anglo-Saxon or Nordic models.

Nevertheless, and that shall be stressed, several similarities with the Anglo-Saxon and the Nordic Model can be made, which also could express the core of the European Social Agenda. By that, the European Constitution delivered a base of common European social values and principles.

Anglo/Nordic Model	Social Market Economy
Flexicurity	Market economy and social stability
Balance of rights and responsibilities	Solidarity on mutuality
Appropriate mixture of individual and collective security	Subsidiarity

3 How can the social model prove its value in real terms? Some benchmark indicators

The European social model is not an end in itself – it is constantly being tested in real terms. Those social models, which pass the test, guarantee the citizens a high degree of labor participation, distinguish itself through high rates of growth and have stable state financing. The countries accept therewith varying amounts of risks of poverty and balance these through social transfers to very different extents. To illustrate this point, the following data is offered.

Criteria of a powerful performance of the Social Agenda are efficiency, effectiveness, equity and sustainability.

Effectiveness and **equity** mean the degree of fulfilled goals. In terms of its **effectiveness** high growth rates and high labour market participation (of problem groups – pensioners, low-qualified workers, and the long-term unemployed) are required. The question of **equity (social justice)** of a social model can be a measurement of the ability to prevent poverty (poverty traps before and after transfers, distribution of income).

Efficiency and **sustainability** measure the efforts that are taken to attain the goals. **Efficiency** can be described by the level of public transfers to achieve better employment participation and poverty rates reduction. Efficiency also deals with the capacity of MS government and business to keep their competitiveness. **Sustainability** means the intergenerational burdens that have to be taken in account concerning the economical and social performance, for example public debt, environmental burdens or fertility rates can be taken into account.

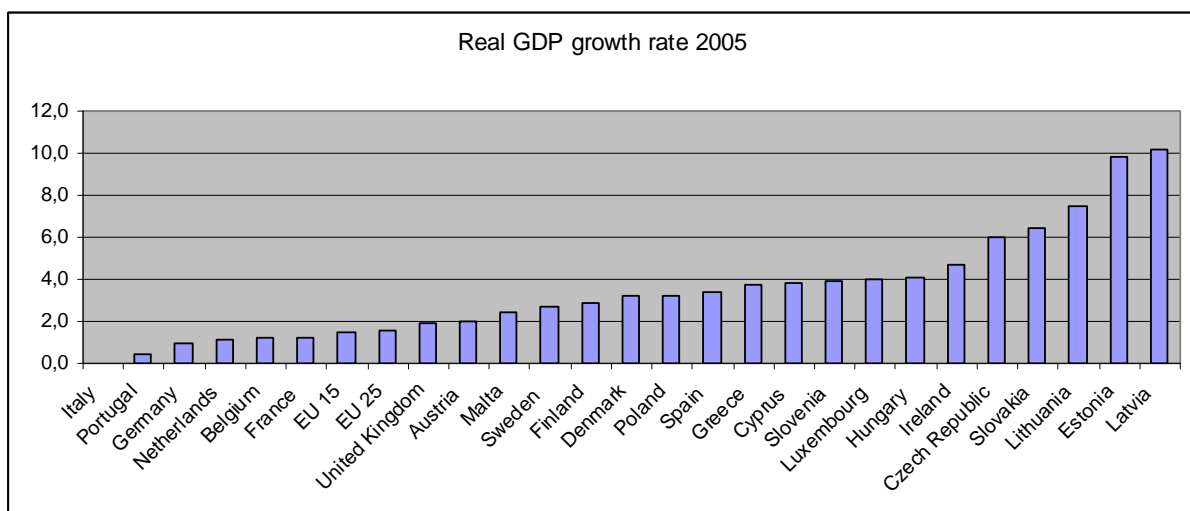
All MS and groups of social models perform differently regarding to these criteria. They stress thereby different social policy approaches and follow different ways to obtain the goals.

In terms of **effectiveness** and the **sustainability** the Anglo-Saxon and the Nordic models are the best suited at present to meet the global challenges.

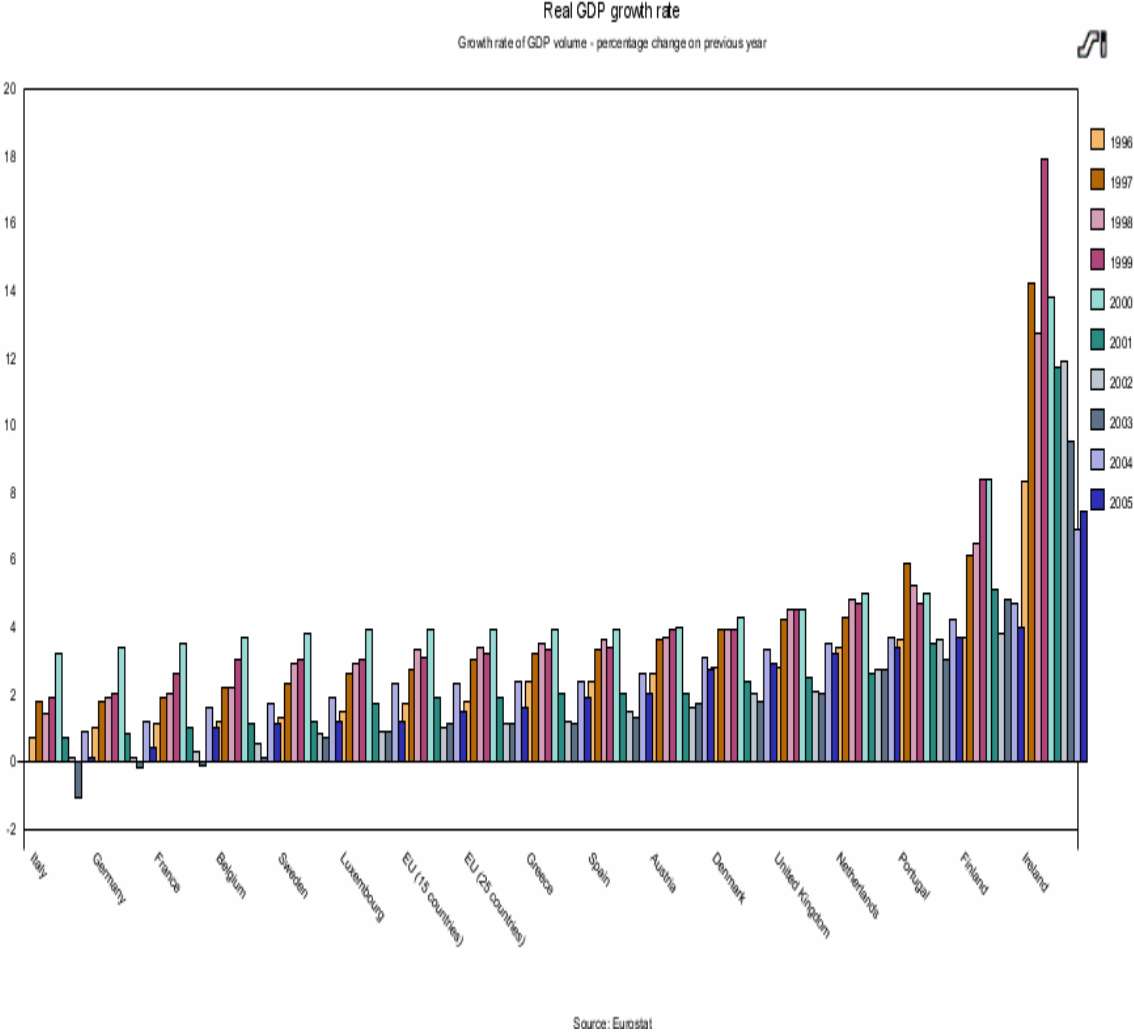
3.1 Effectiveness

1. Real GDP growth rates

Regarding the real GDP growth rate 2005, the Continental European countries perform worst.

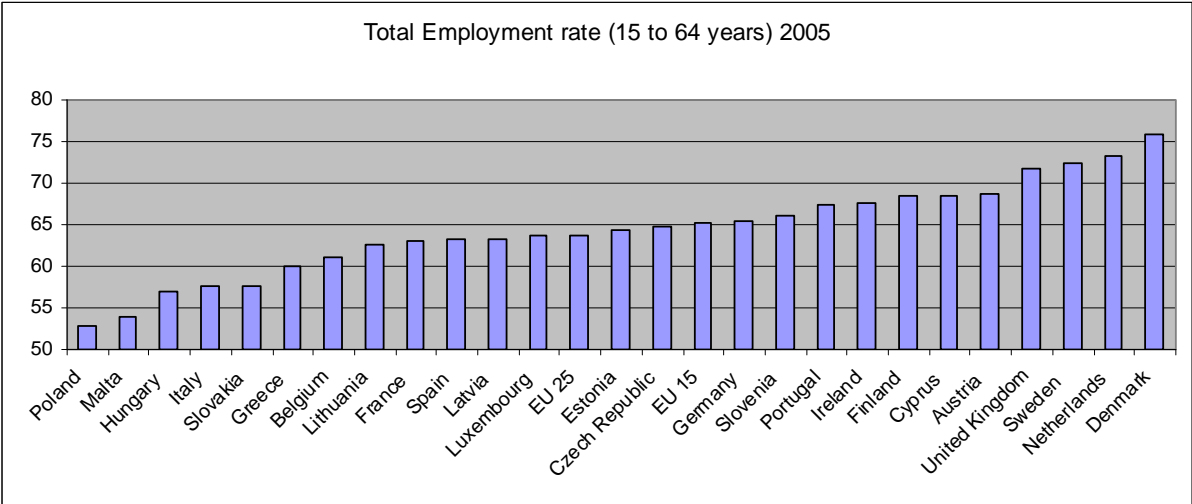


The last ten years (1996 to 2005) underline the growth problems in the highly populated continental European countries.

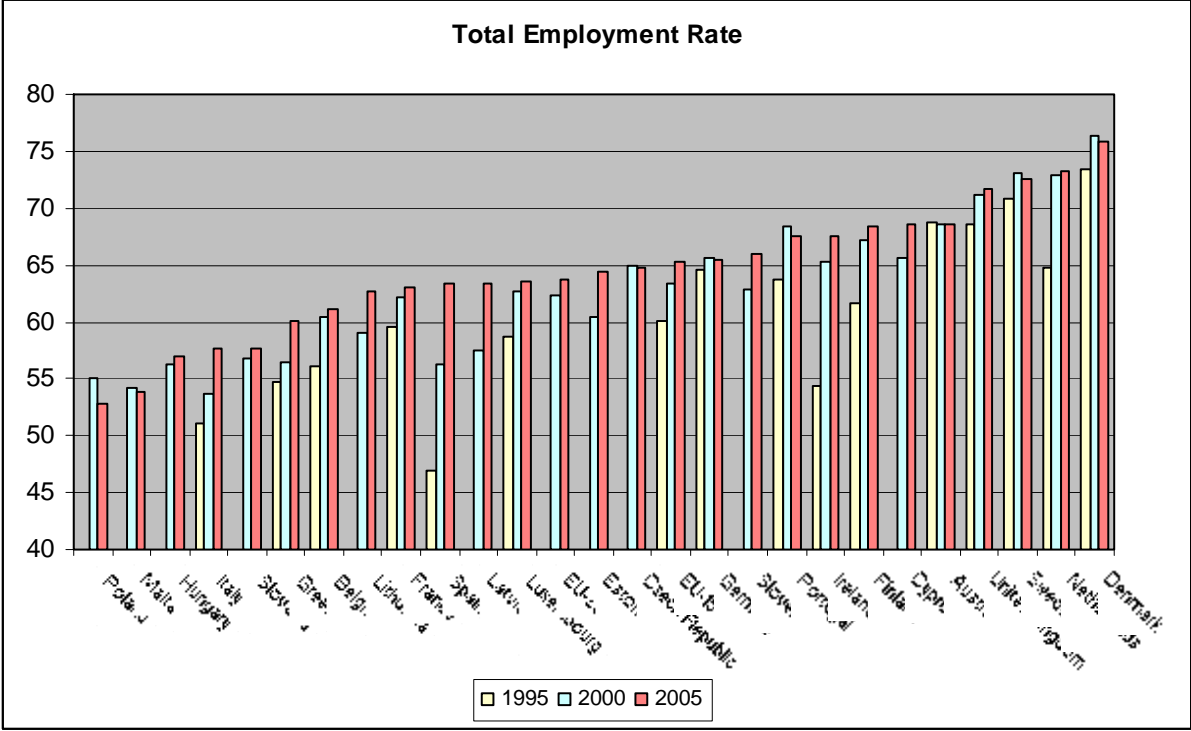


2. Employment rates

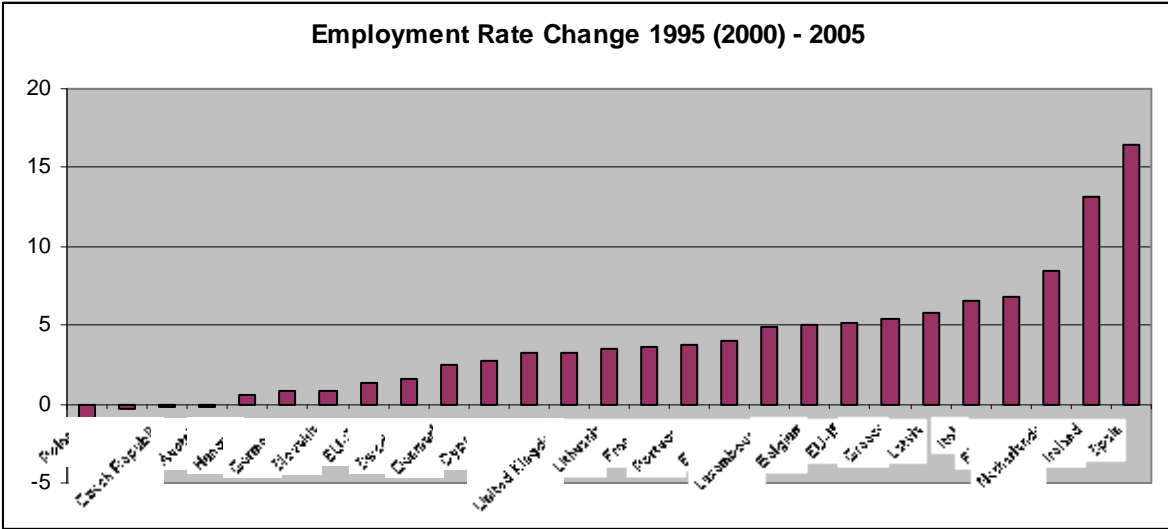
The total employment rate 2005 stresses the good results of Nordic countries.



The following graph shows the development of total employment rates in the last 10 years, selected by the employment rate in 2005:

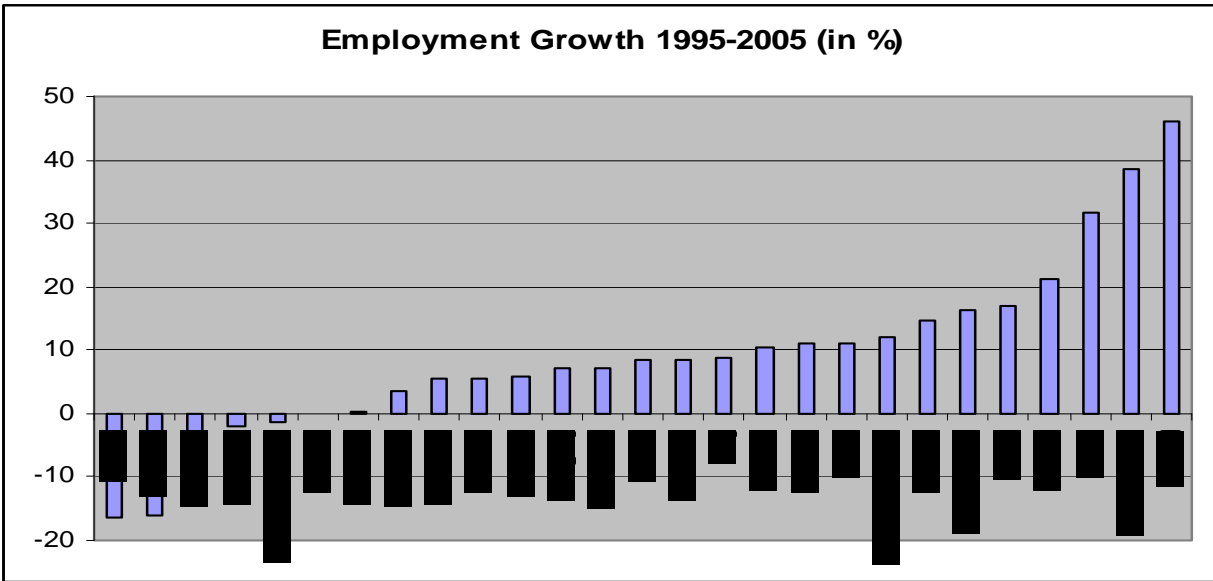


The difference of the employment rates between 1995 and 2005 (new member states 2000) shows the next graph:



3. Employment growth

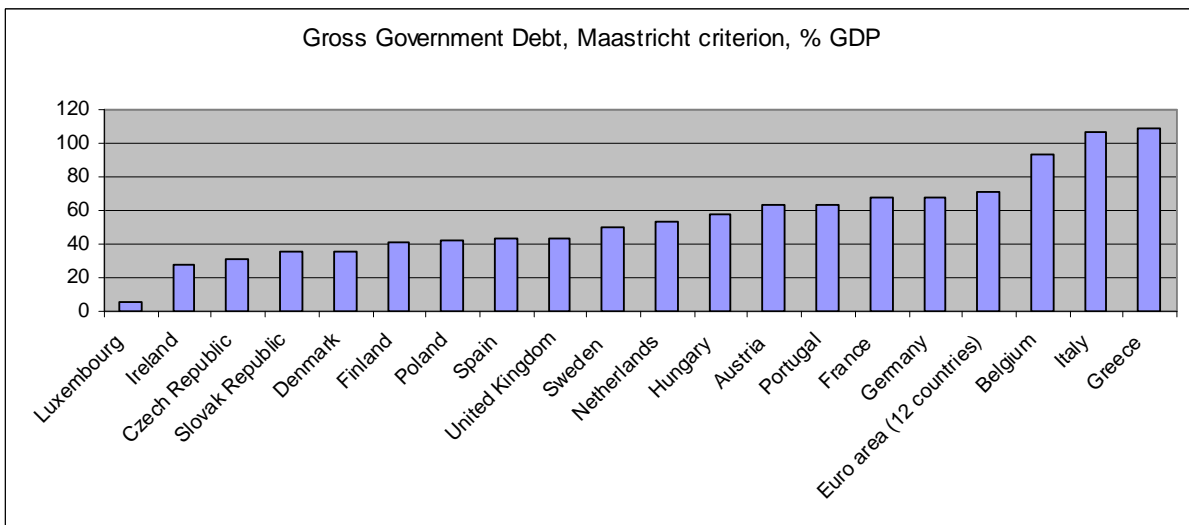
A further indicator for the effectiveness of the social model is the capacity to create jobs – measured by employment growth. The next graph points out the overall growth rate between 1995 and 2004. No clear ranking within the different groups can be observed.



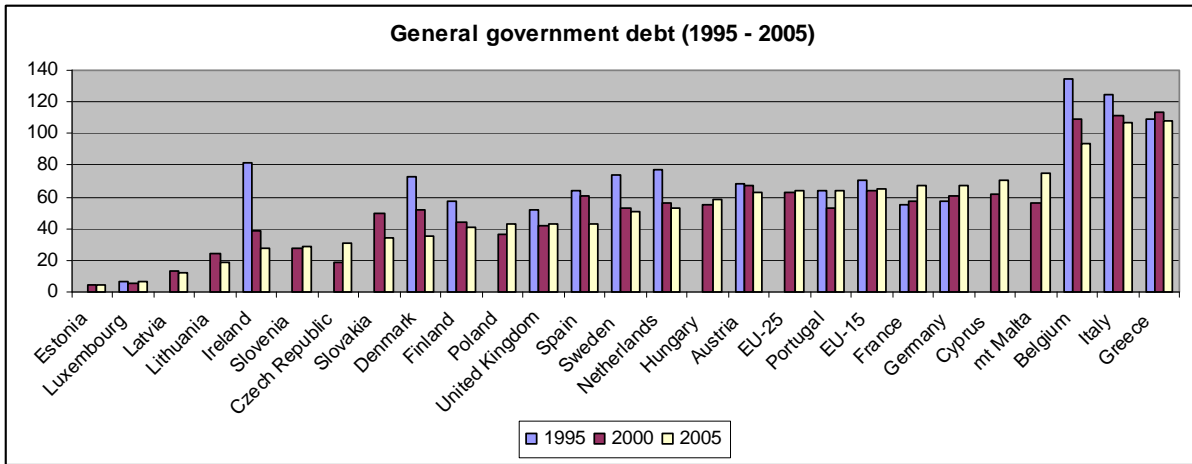
3.2 Sustainability

1. Gross government debt

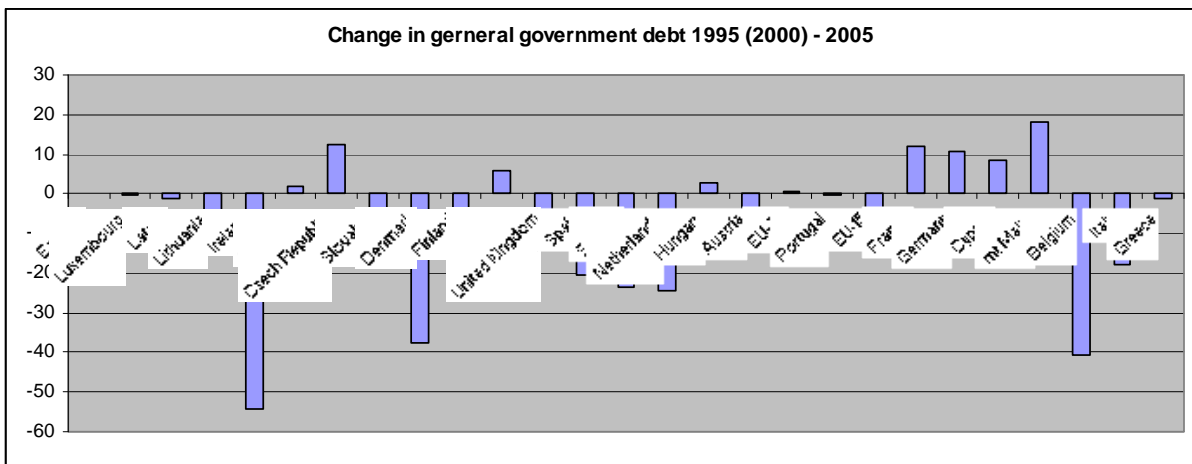
Concerning the sustainability of the social models, we can look at the overall public debt. The less sustainable models are the Mediterranean and continental countries.



Following the last 10 years, the gross government debt only raised in France and Germany, in all other countries, there is a significant reduction to consider (new member states not considered).

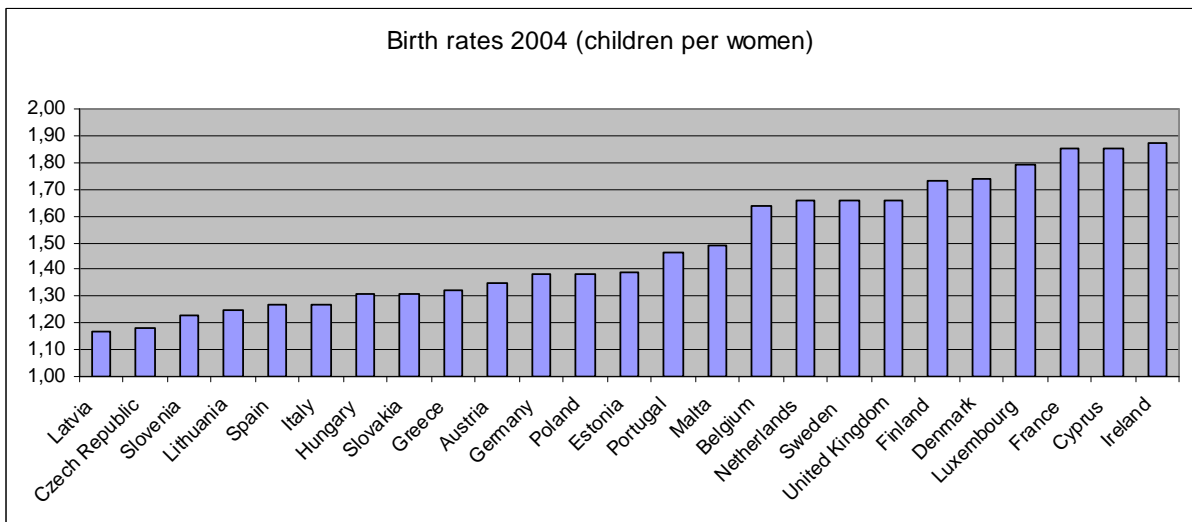


The difference of the general government debt between 1995 and 2005 (new member states 2000) shows the next graph:



2. Birth rates

The comparison of birth rates also gives a picture of the sustainability, for “children” either express hope and future or younger societies shall better be prepared on future change.

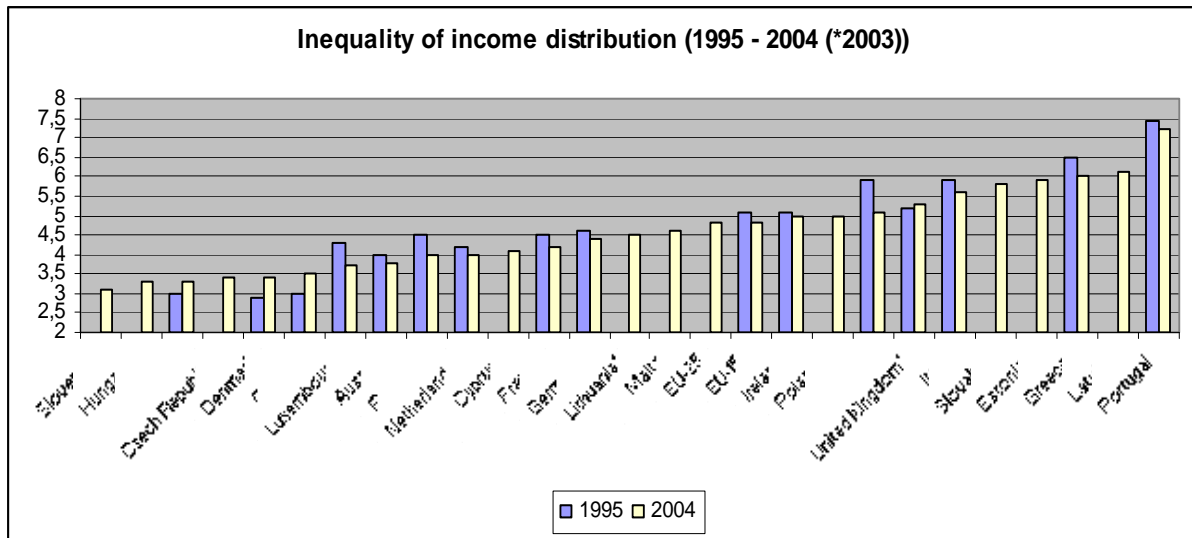


3.3 Equity

In terms of **equity**, the Nordic and Continental European models have thus far led to better results than Anglo-Saxon and Mediterranean models.

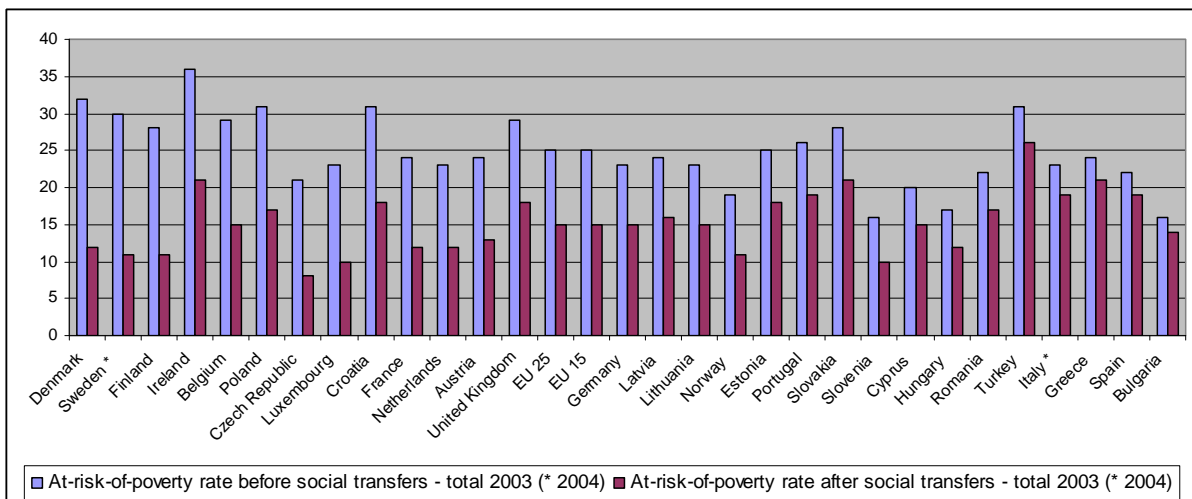
1. Inequality of income distribution

The inequality of income distribution (income quintile share ratio) is less in Nordic and continental than in Anglo-Saxon and Mediterranean countries. Nevertheless, comparing the last ten years, all other countries were able to reduce this ratio exempt the Nordic countries.



2. Poverty risk

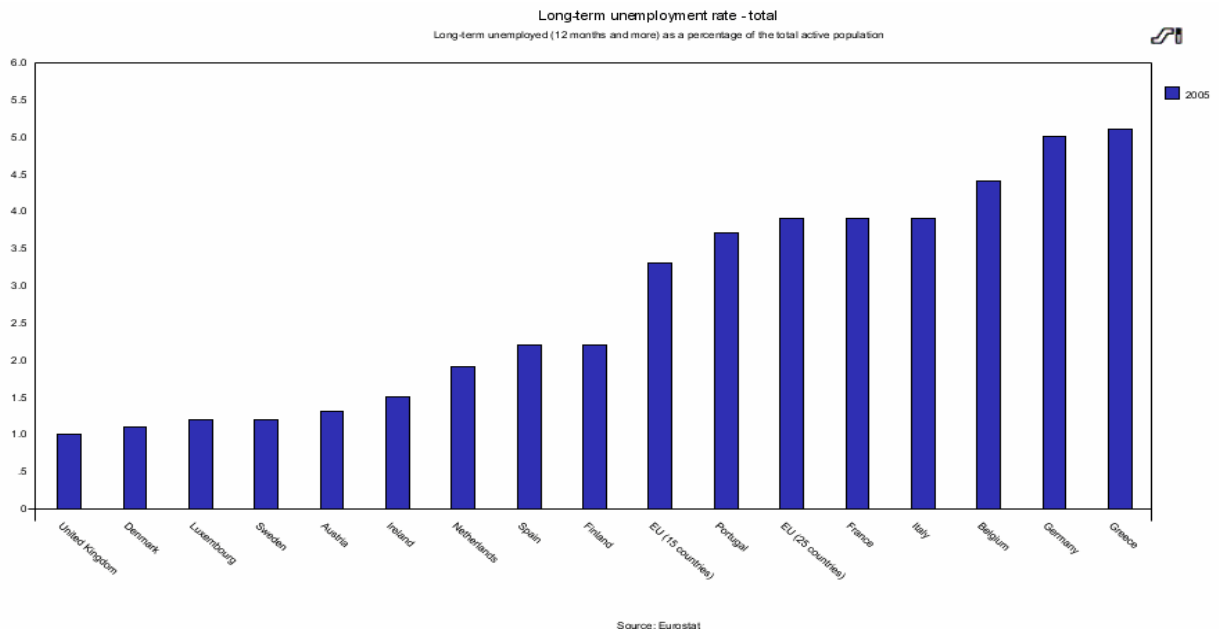
Having a look at the poverty risk before and after social transfers, the strong performance of Nordic countries is obvious.



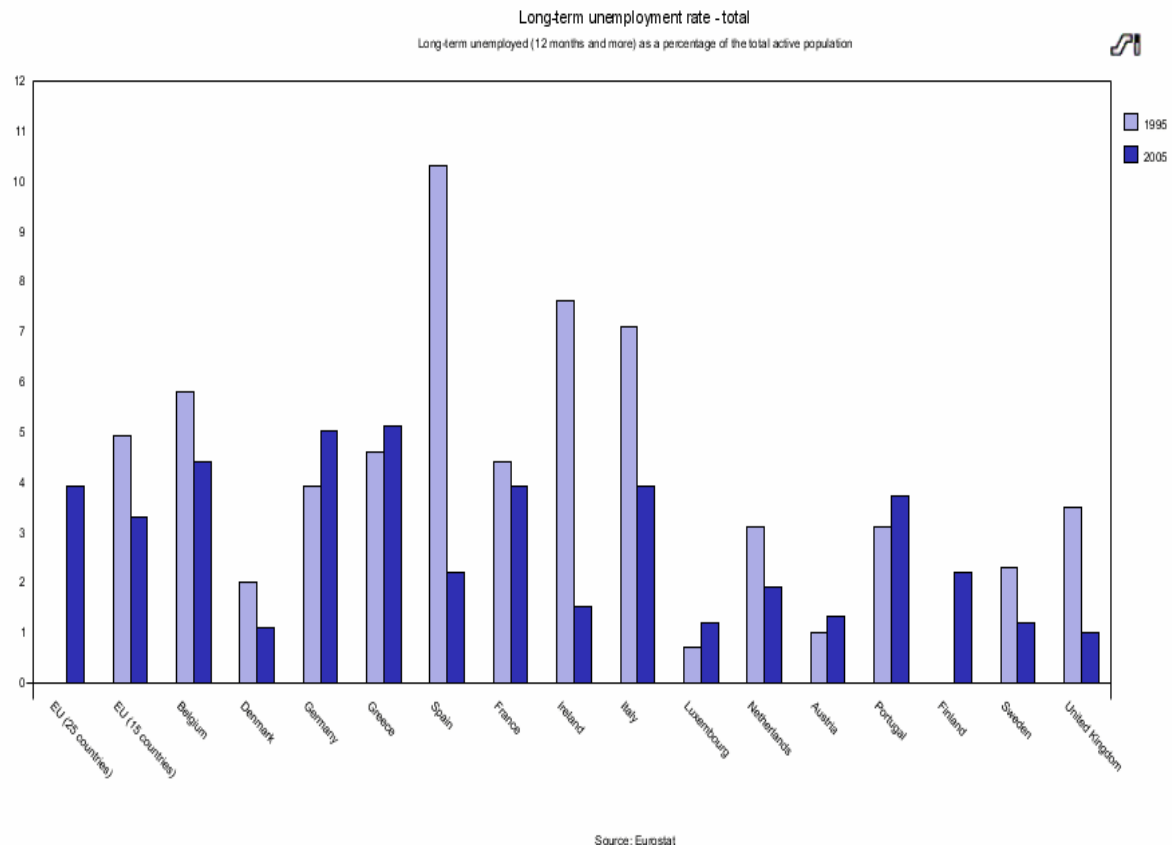
3. Long term unemployment

As employment is the key of wealth and participation in all European social models, the fact, being locked out of the labor market is a fundamental criterion of equity.

The Nordic and Anglo-Saxon model show the best performance.



Concerning the development of the last 10 years, the next graph stresses the data of the year 2005. We consider a very strong reduction in Spain and Ireland and an increasing numbers only in Germany, Greece and Portugal.



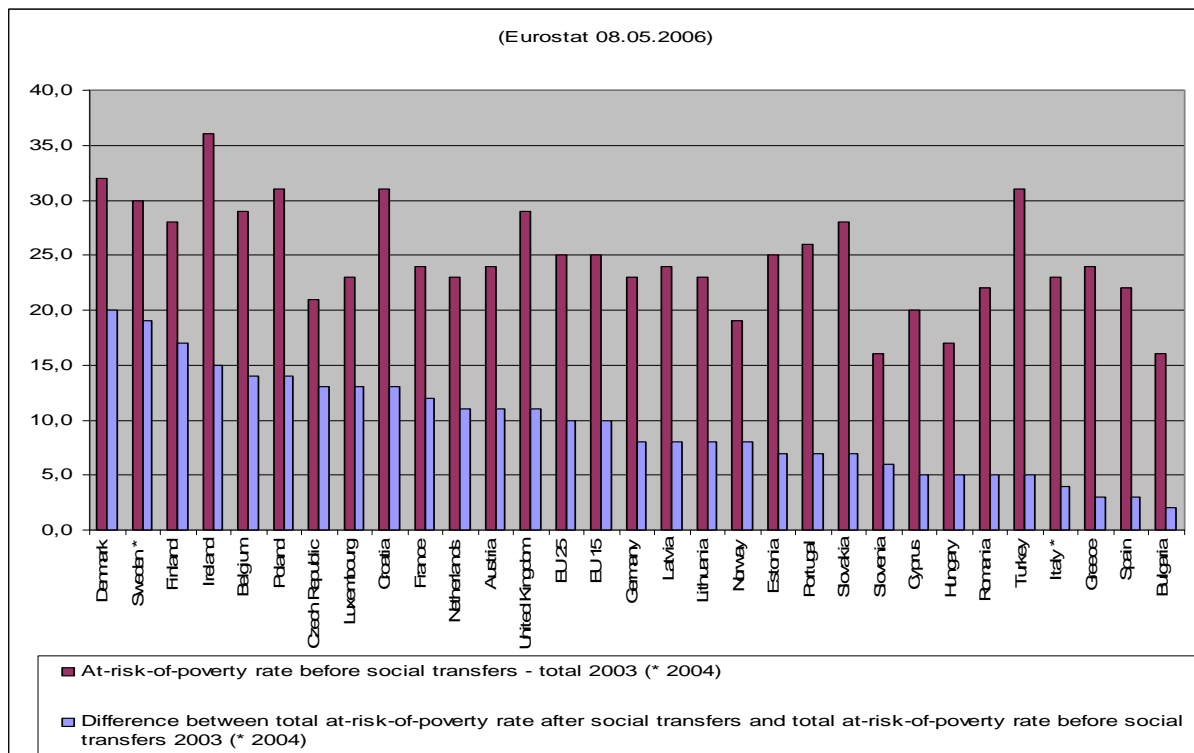
3.4 Efficiency

1. Efficiency of social transfers by reducing poverty risks

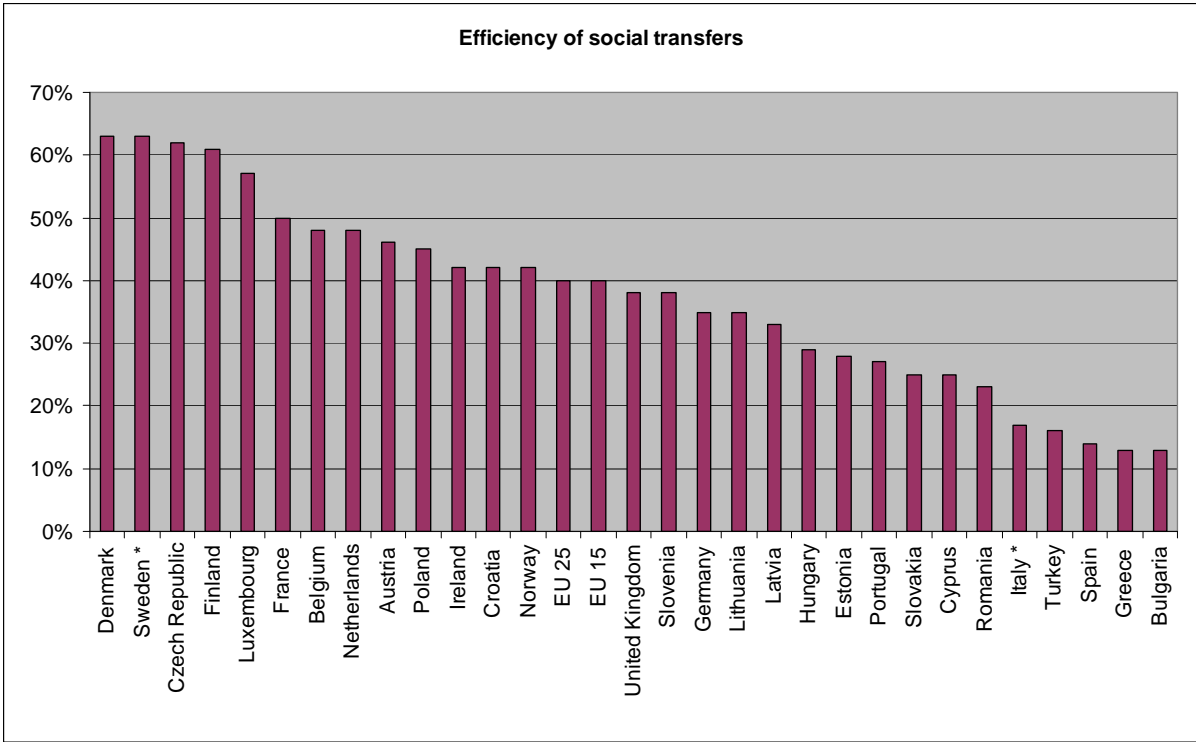
The question of **efficiency** of the various social models, however, should not be answered merely with the itemized criteria (see above) found under effectiveness and sustainability (which Sapir tends to do in his report).

Because the efficiency of a social model provides not only information about the degree to which goals are reached, but also about how the goals (effectiveness, sustainability) are reached (which consequences (i.e. trade offs) are accepted in different countries).

Next figure orders the countries after the absolute reduction of poverty risk by social transfers.



In relative terms, the next figure measures the degree of reduction by social transfers. The absolute reduction is divided by poverty risk before social transfers.



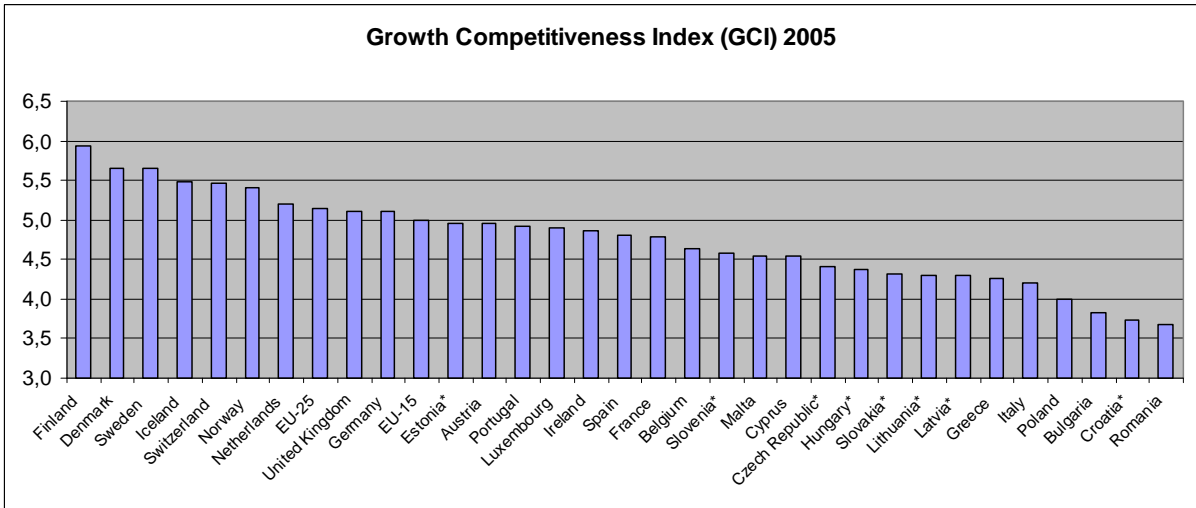
Finally social expenditures as input of the social model can put in relation to the absolute risk reduction by social transfers. Therefore, we can Here the question of the social model’s influence on a country’s ability to compete arises.

2. Effects on competitiveness

Two indices of the World Economic Forum are drawn on as a starting point: the Growth Competitiveness Index (GCI) and the Business Competitiveness Index (BCI).

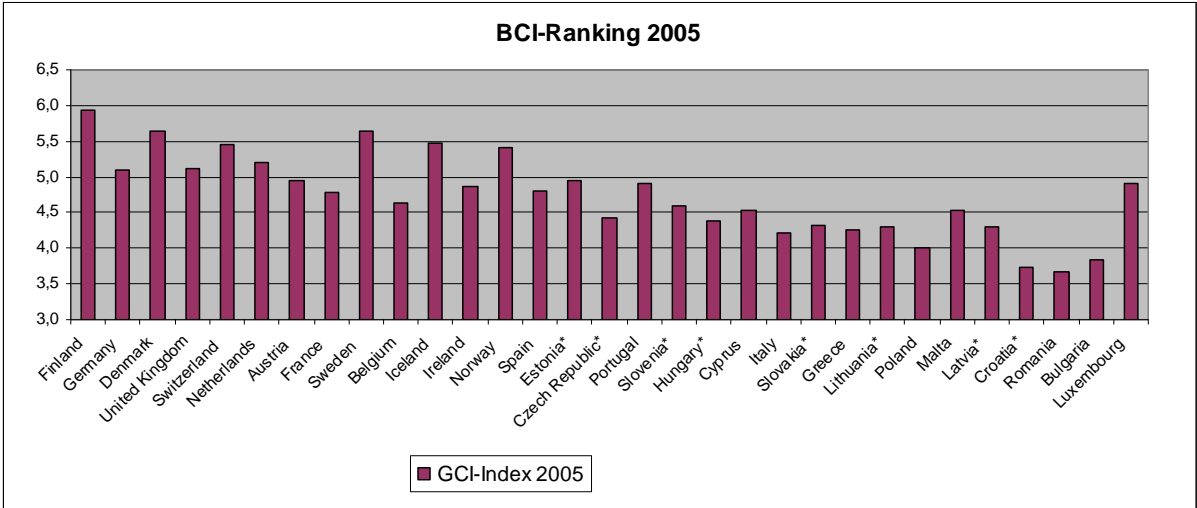
The GCI tries to express facts about the factors that drive competitiveness in a country: quality of macroeconomic environment, state of public’s institutions and the level of technological readiness.

According to the GCI, the Nordic countries are the most competitive in the world. The degree of social protection practiced there is obviously no obstacle for relative competitiveness.



The BCI focuses on the underlying microeconomic factors which determine economies' current sustainable levels of productivity, since wealth is created on the level of the firms operating in an economy and competitive companies are a good basis for the sustainability of a social model and thereby rounding out the entire impression.

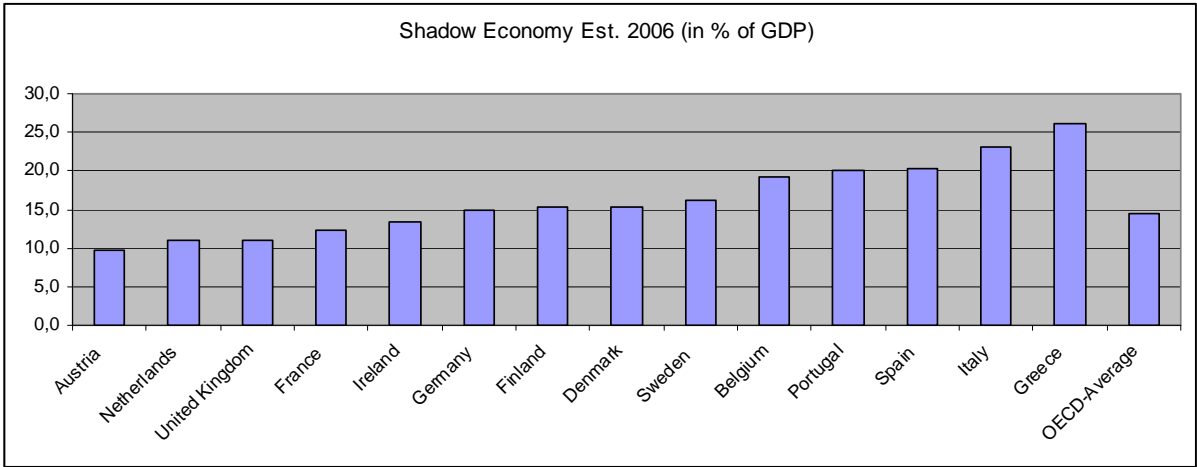
Neglecting that the United States are number one listed, next figure follows the ranking of BCI from position 1 (Finland) to position 78 (Bulgaria). (Luxemburg was not listed in the BCI).



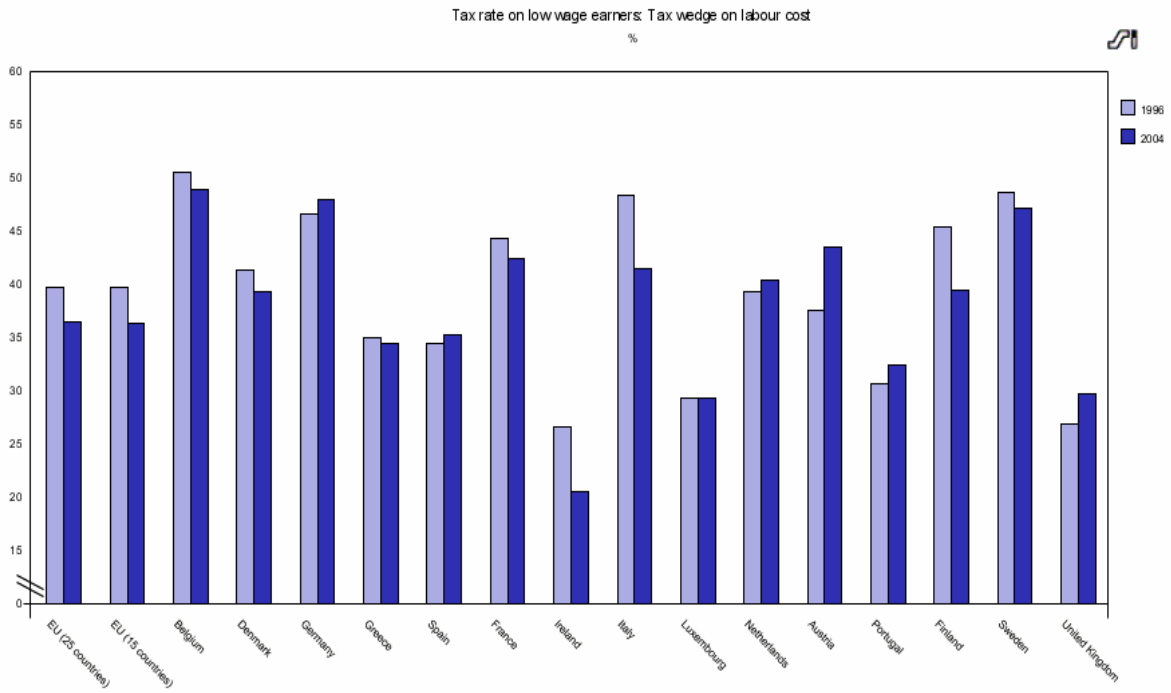
Following the BCI index some Continental European countries obtain somewhat better results than individual Nordic or Anglo-Saxon countries.

3. Shadow economy and tax wedge on labor costs

Telling of a social model's efficiency is also the size of the **shadow economy**. In this regard, the Nordic countries and the Mediterranean countries above all do poorly, while the Anglo-Saxon Model and the Continental European model including the Netherlands and Austria fall significantly under the average shadow economy contingent of OECD countries.

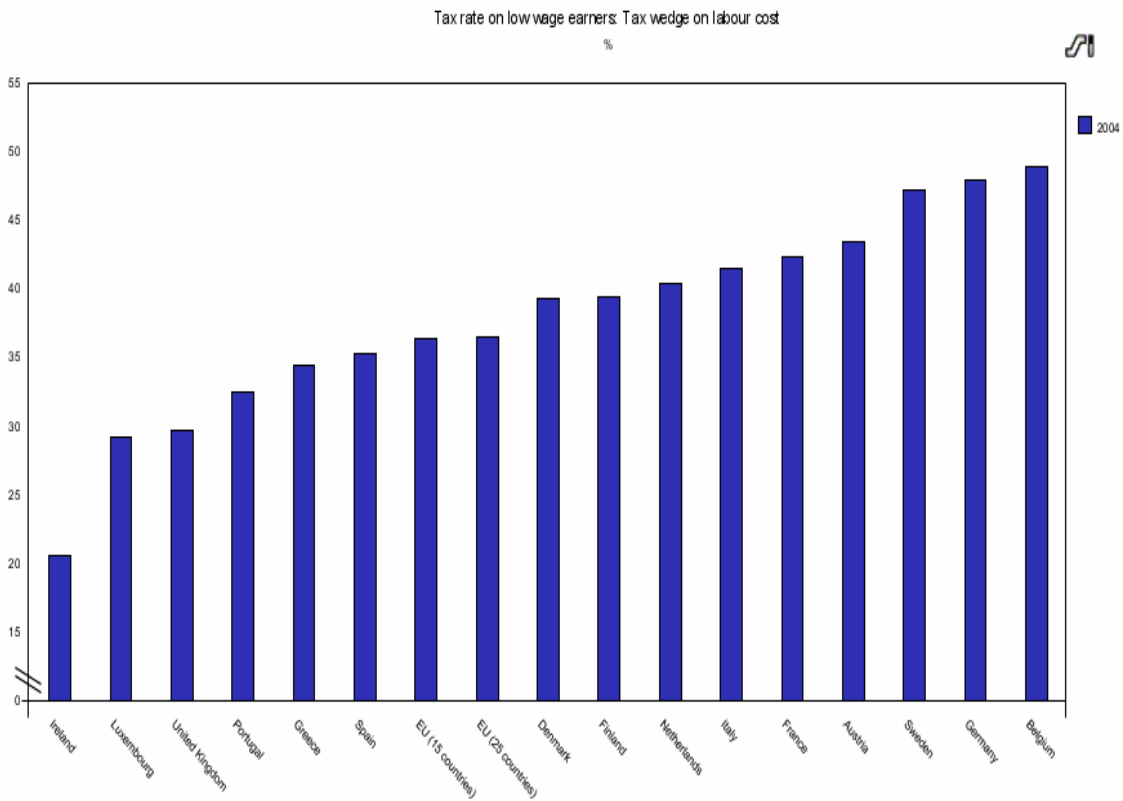


On the other hand, European social models deal with the fact of adjusting individual responsibility and collective contribution. One special criterion defines this border of individual and collective allocation: the tax wedge (tax rate on labor). It clearly points out, at which point, the society adjusts individual and collective responsibility.



Source: OECD, Commission services

First of all, we can observe, that with exemption of the UK and Portugal, all countries reduced the tax wedge in the last ten years.



Source: OECD, Commission services

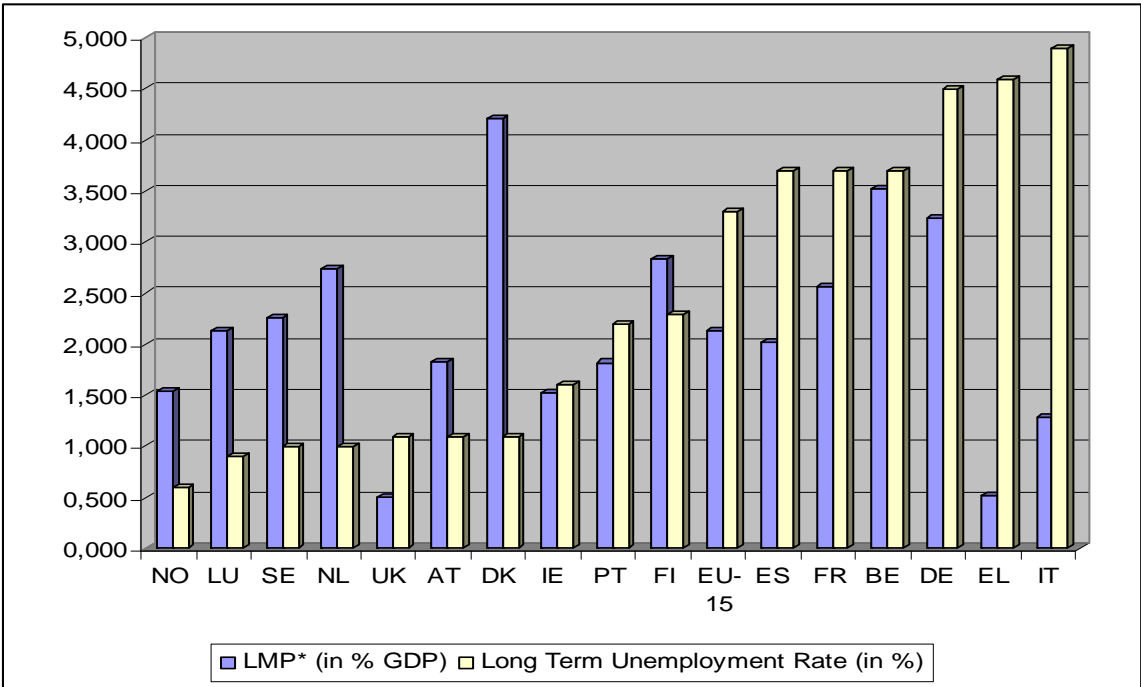
Otherwise, the graph clearly stresses, that Anglo-Saxon countries leave the clear majority of incomes in the sphere of the individual, while continental and Nordic countries have high tax wedges to strengthen collective approaches of responsibility.

Labor market policies

Alongside general indicators of efficient social policy, the following graph gives a specific look to the efficiency of the labor market policy by connecting expenditures of labor market policy (LMP) and long-term unemployment rate in some countries.

Nordic countries achieve comparable success in the labor market participation with a greater interventionist labor market policy than the Anglo-Saxon countries. The inefficiency of the large Continental European countries like Germany and France is likewise evident.

Thus should be a question of systems – meaning institutional arrangements as an expression of a value and political system – and of policies inhibiting the proper functioning of labor markets. Systems are less easy to change than polices – and the message to politicians could be look first at the policies.)



3.5 Results of Benchmarking

As a result, it can be seen that there is not an explicit relationship between the social models and the competitiveness of countries and its businesses.

Overall, the comparison of single Member States argues for better performances by the Anglo-Saxon and Nordic models and thus for the thesis of *Andre Sapir*. Both model groups are leaders in the questions of growth, participation in the labor force and unemployment in Europe. That being said, countries which adhere to the Continental European model, like the Netherlands or Austria, can also keep up and achieve better results than the Anglo-Saxon countries with respect to sustainability and the equity of its social model.

In light of the manifold basic options and diverse institutional transformations, the question which country solves its problems the best is not so conclusive and easy to answer as Sapir's thesis suggests.

Rather, the countries and systems must first be differentiated and looked at separately in order to then be compared. In this regard, one only has to think about the marginal foreigner contingent among the population in the Nordic countries. The Nordic countries, however, along with the Netherlands and Austria have demonstrated that good basic economic data and a high degree of competitiveness can be united with an efficient and social safeguarding.

When naming archetypical countries, it should not be forgotten that neither Sweden nor Great Britain were among the model students in the 1970s and 1980s and were considered patterns for the future at that point.

Over the past 15 years, a consistent trend has emerged in all countries with the level of social benefits in the various countries decreasing. A limited convergence can also be recognized on the side of financing with the degree of employer contribution dropping as well (compare above the table of social indicators).

4 Conclusions and Recommendations for a EPP/ED appropriate answer to the future of a European Social Agenda

4.1 The direction of economic and social reform

All countries in Europe have profited from citizens feeling a sense of (social) security, with social peace flanking societal change. The respective social models can function inclusively and preventatively, so that the individual has little to lose. A small regulated free market economy contributes to competitiveness – the Nordic states are a good example of this. If the social state supports participation and social advancement, above all through active and fair entry to work and education and training (and is therewith effective), then a division of society into winners and losers of modernization can be avoided. Social security is to a certain extent preventative. The welfare state and competitiveness must not be played off against one another; rather, per se “growth [has] nothing to do with the level of social expenditures.”

But the border between preventative and repressive social protection, however, can be blurred. If social policy transgresses the line which balances the chances and risks of a free market economy with social equity (compassion), market distortions, welfare loss and a loss of competitiveness arises. This is regularly the case when the social security for specific groups is over emphasized and in effect the protection norms turn against the group being safeguarded.

Which concrete characteristics of the social model are harmful to broadly invested prosperity development? Many studies on the consequences of public welfare plans have sought to answer this question. According to many of them, far reaching social security systems are not per se inhibitions to growth, production development or increased prosperity.

Every European member country has experienced a phase in its history when it has overstepped this line. Thus, no Member State is immune to overstretching the extent of social, collective financial security. Yet, no state lacks all hope or prospect in finding its own way to a well-balanced relationship between the two either.

The common principles of a European Social Agenda are not an end in itself; they need to contribute to good economical and social performance in MS. By that, the European Social Agenda would stress the capacity of permanent economic reform (adjustment). That does not mean more competence at the EU level; but more compassion on a political level in translating the values of a European Social Agenda into the national context.

4.2 Define values and principles of European Social Agenda and economic reform

The European Social Agenda as a common Social policy approach – not a common unique Social model – is based on the same understanding of human being with untouchable dignity. All European Member States (MS) agree that competition as the source of wealth and growth needs a legal frame work. Therefore the European Single Market has to be completed.

All MS stress the meaning of national social policies, to reduce poverty and to help people with the aim that nobody shall be left alone in the process of globalization. Social security shall be provided by public institutions – not because of repairing the unwished results of free market economies, but because social protection can raise competitiveness. That means in concrete:

- Collective social security systems are provided against the risk of unemployment, health and aging
- Markets Regulations to stabilize their functioning
- Public training and education systems
- Acceptance of the role of the social partners in national context
- Minimum standards of living according to national wealth

Europeans that have the impression, that MS can not provide a certain level of social protection, will reject the European process. This is one lesson of the referenda in the Netherlands and in France. People do not refuse change, people refuse uncertainty. This is the point, where the European Social Agenda can fulfill an important role.

4.3 Respect different understandings of the role of the State/Government

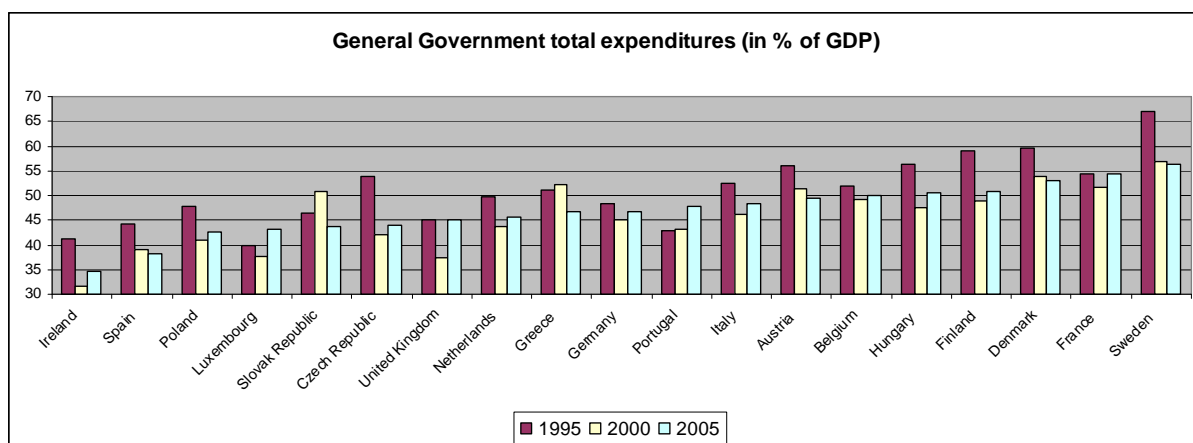
The role of government and state highly differs. All MS deal with a mixture of individual and collective approaches of their social protections. Europe's Economic reform and its Social Agenda will not be successful in staging Europe as an island of the holy that is far away from globalization. Because of that, all MS should adjust their Social models in a more individual and less collective direction. Most of the MS already went in this direction – some go further than others (and some cannot go as far as others can). The deep differences in the understanding of the role of government and state have to be considered in all recommendations of reform a European Social Agenda.

In the Nordic countries, this fundamental principle is strengthened by a high degree of state trust. The Nordic populations have a pronounced willingness to contribute to a functioning political system. The high rate of unionization has also become a supporting pillar of this state conception. **“Self refusal”** is not accepted in society. In addition, the state benefits recipient continues to belong to the community of solidarity. The handling of wage compensation serves as evidence for this thesis: in Denmark wage compensation is subject to taxation while in Germany it is presented as tax-free income. Thus, the Danish, in contrast to German, unemployed continue to contribute to the financing of the state.

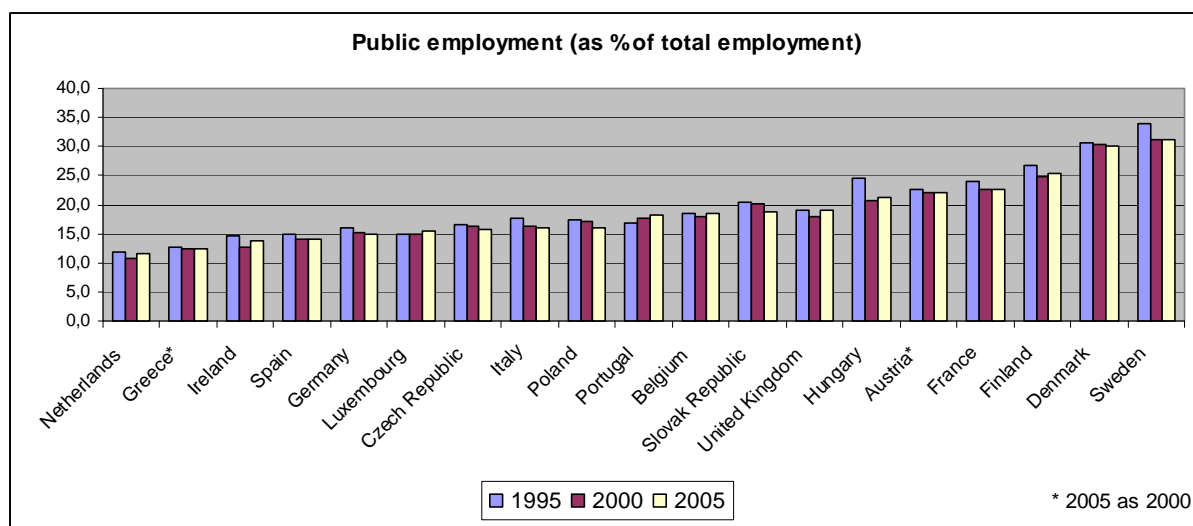
In the German system, the link between continued support of state benefits and unemployment compensation is severed.

In the Anglo-Saxon countries, a similar effect is produced, but in a different manner. The overall amount of state benefit is lower than in the Nordic countries and, yet on par with the Continental European countries.

The different level of the state can be measured by the general government expenditures an all levels of the state. We can observe a clear reduction in nearly all member states with Nordic and continental European countries still underlying the important role of the government.



The different role of public institutions also shows up in the part of public employment on total employment.



It seems that the Nordic models perform especially well in regard of employment rates by stressing the role public employment. That “way of success” for instant could cause deep problems of acceptance in many other European countries.

Is there a need for harmonisation of (minimum) social standards amongst EU member states? What differences in social security levels are still acceptable?

After two years of experience with the 10 new MS, we can not state a relevant flow of people from new to old countries because of higher social standards – but because of job opportunities. The social level must accord to the MS economical capacity and depends on the culture and the decision of voters in the governmental elections.

All taken into account, common principles and common public task should be stressed as one of Europe’s contributions to a better world and the solidarity with non-EU-mebers. But the fixing of concrete social minimum standards (for example the level of social help/welfare) would over-stress the project.

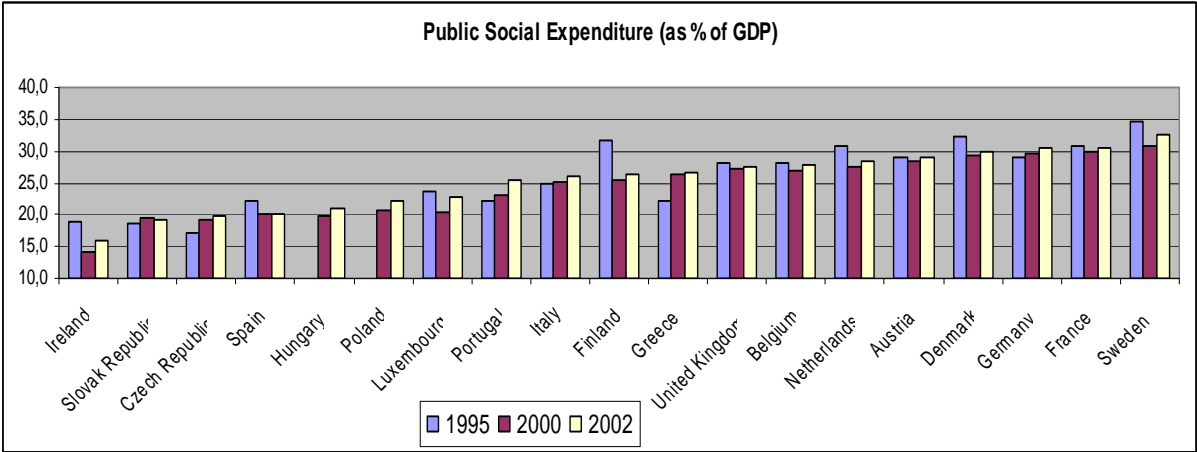
4.4 *Stress the investive character of Public Expenditures*

If the social expenditures in a social security system (health insurance, labor market policy) focus on health recovery or a specific reintegration into the labor market, then it creates the basis for participation in the competitive process. If the public sector provides a high level of education, then the positive incentives for competitiveness and prosperity cannot be disputed. One can speak of a preventative or **investive** social model. Social models, which satisfy these criteria, incidentally find a large acceptance among taxpayers for the financing of benefits for the deserving.

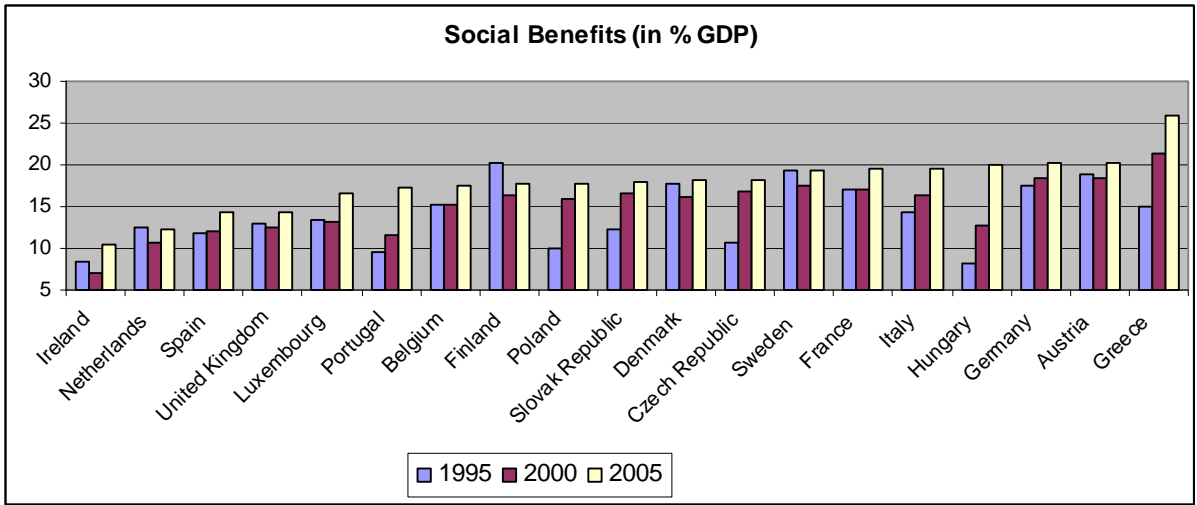
If the character of the social spending however rests on consumptive transfer services, then the social model paralyzes creative forces and competitiveness. In addition, state subsidies used to protect specific jobs and sectors, or regulations which separate and bulkhead individual industries also figure in this respect. In these instances, the negative influence of social levels on competitiveness prevails, as the market principles are distorted.

Consumptive Expenditures

First having a look at the total public social expenditures, we can observe the strong role of social policies in Nordic and Continental European countries.



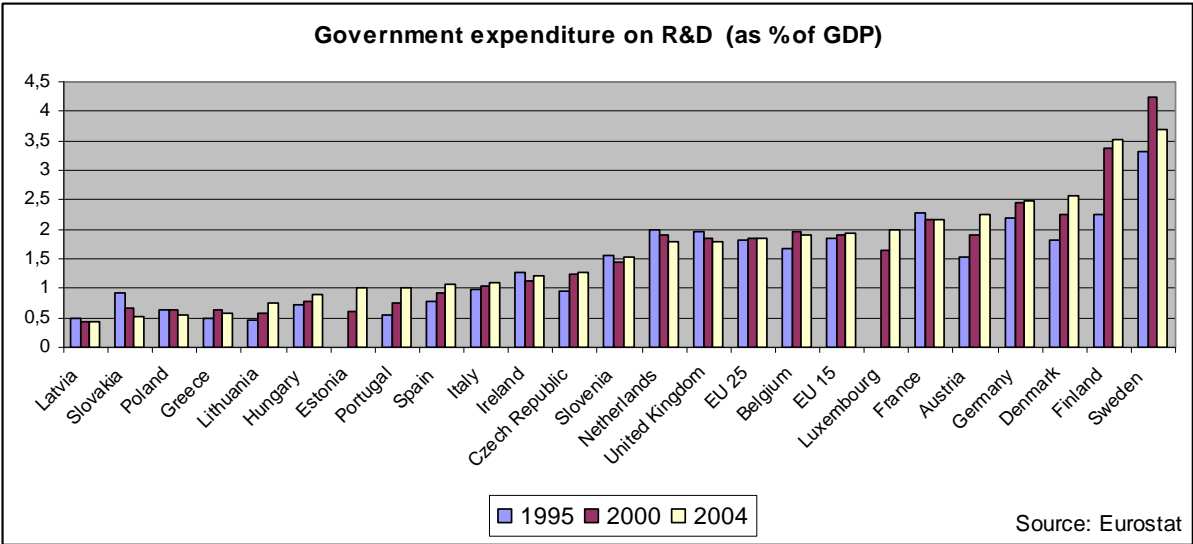
Focusing in a second step on the rate of social benefits which stress the consummative (transfer) character of the social model, we can realize that Nordic countries reduced that volume in the last years and are ranked in the midfield of all countries.



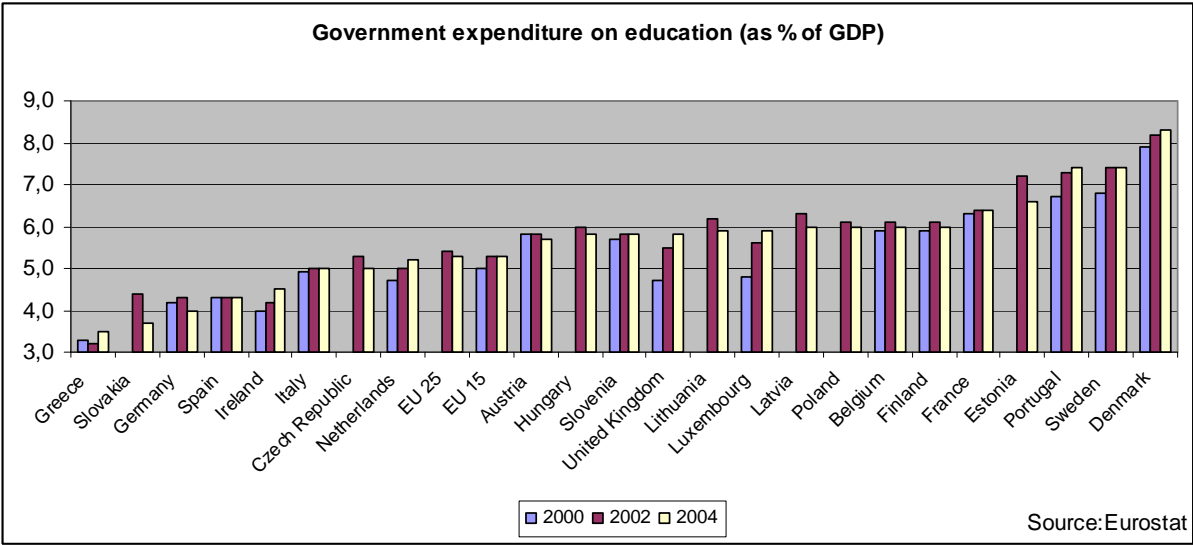
Investive Expenditures

The special preventive and investive character of the social models shows up in public expenditures for research and development and education.

Expenditures for R&D are the highest in Nordic countries, followed by Continental European states.



Turning on to expenditures for education, we can observe similar results. The Nordic countries stressed the meaning and importance of public expenditures in education.



The further role of education, formation and knowledge shall as key point of powerful European economies and social cohesion with high social standards (“Social protection by better education!”) can be derived from the two graphs above.

4.5 Reduce barriers for the success of the Lisbon Agenda Process by focussing on labour market participation

The core of a successful European Social Agenda will be the fulfilling of the Lisbon Agenda goal “more and better jobs”.

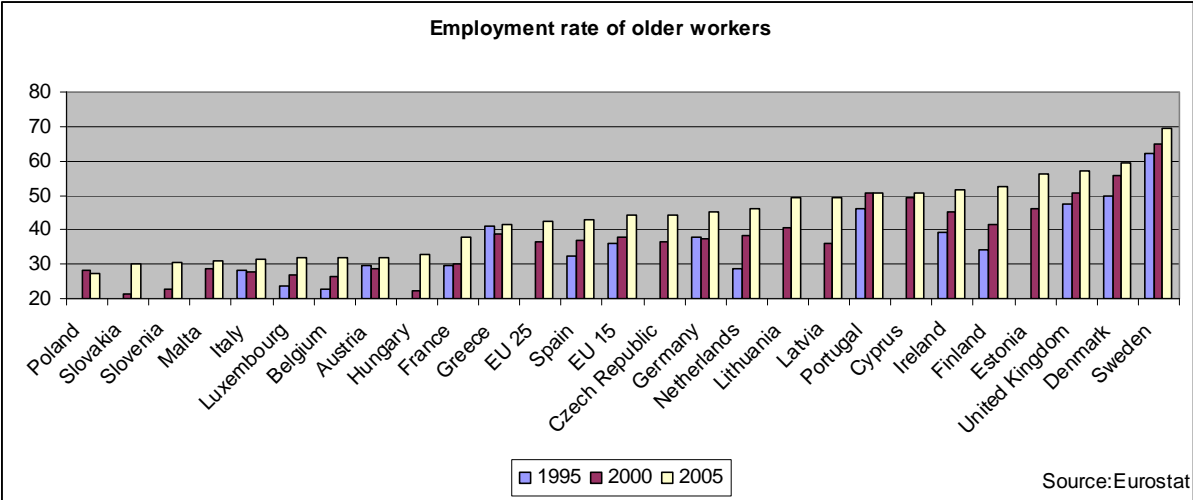
There is no such thing as a functioning Social Model with 20 million people unemployed and 80 million people inactive in Europe. With more and better jobs, other goals like growth and poverty reduction will be achieved with more simplicity. In this area, there is no and probably should not be a European responsibility. Nevertheless, the European level could focus on placing MS adjusted messages to these special topics.

The following points stress labour market integration and thereby strengthen the performance of the social model.

Labour market integration of older workers and other problem groups²

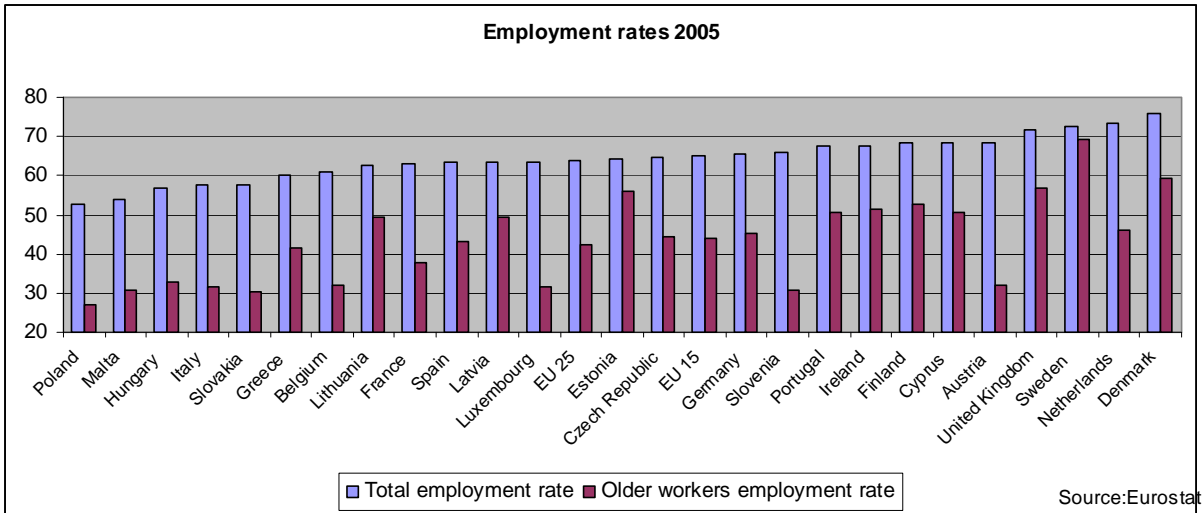
All special labour market programmes to lift the employment opportunities of special groups (older and younger workers, women, low skilled) reduce de facto their employment possibilities. By that, the “2+3+2-regulation” should find an (early) ending before 2011.

The following graph shows the development of the total employment rate of older workers. All countries were successful in raising the rate, but Nordic and Anglo-Saxon countries do especially well.

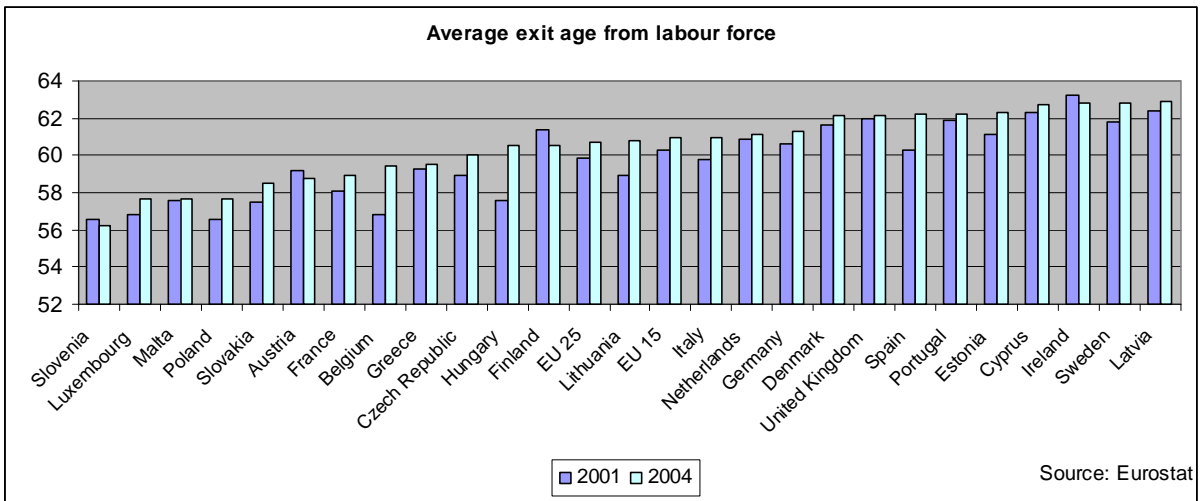


Putting total and older worker employment rates together, we can see that Nordic and Anglo-Saxon countries do the best to force long duration of employment.

² Concerning low-skilled workers, we refer on our paper of last years European Summer School.



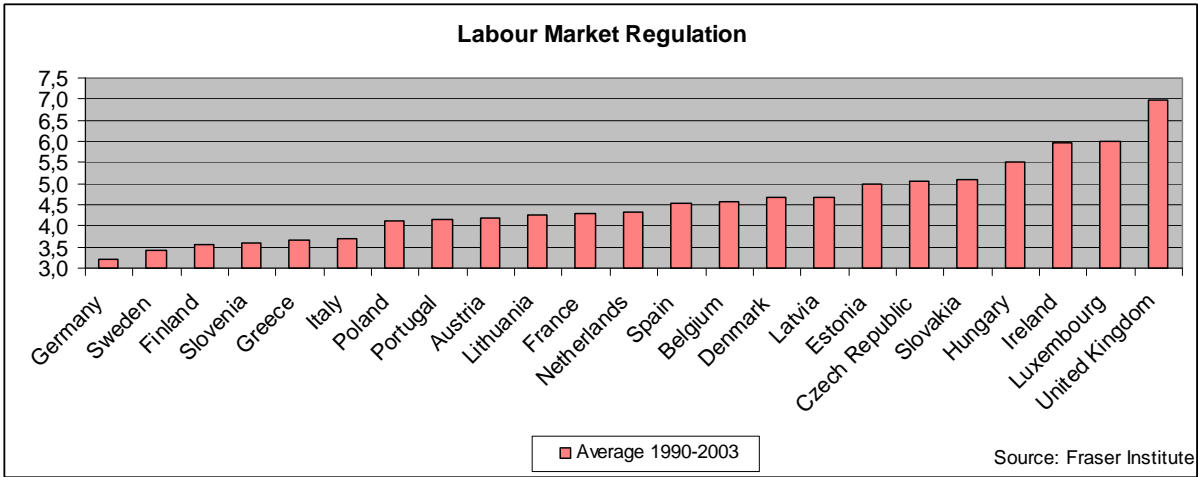
The exit age of older workers also gives a clear sign:



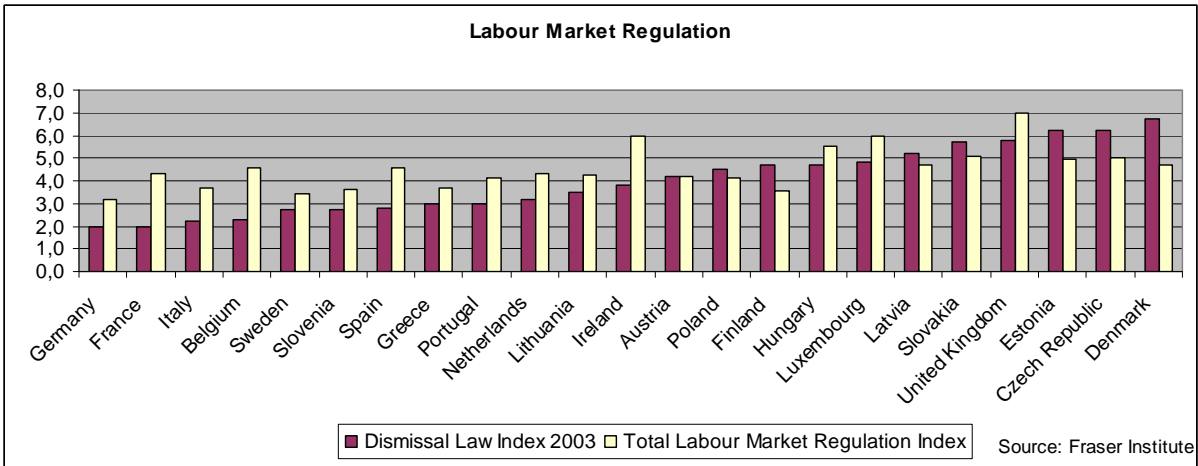
Labour Market Regulation

Higher labour market participation is often linked to less labour market regulation (not any regulation). Decentralized wage negotiation (with opening causes) help to adjust the wage level on the firm's actual economic performance. Dismissal law protection reduces the incentives of employment and should be treated with retention.

The following graph shows the average index of overall labour market regulation between 1990 and 2003 (The Fraser Institute). The highest regulation is linked with the smallest index value and vice versa. The small regulation in Anglo-Saxon countries must be stressed. Nevertheless, Nordic countries do not perform as small regulated as often called.

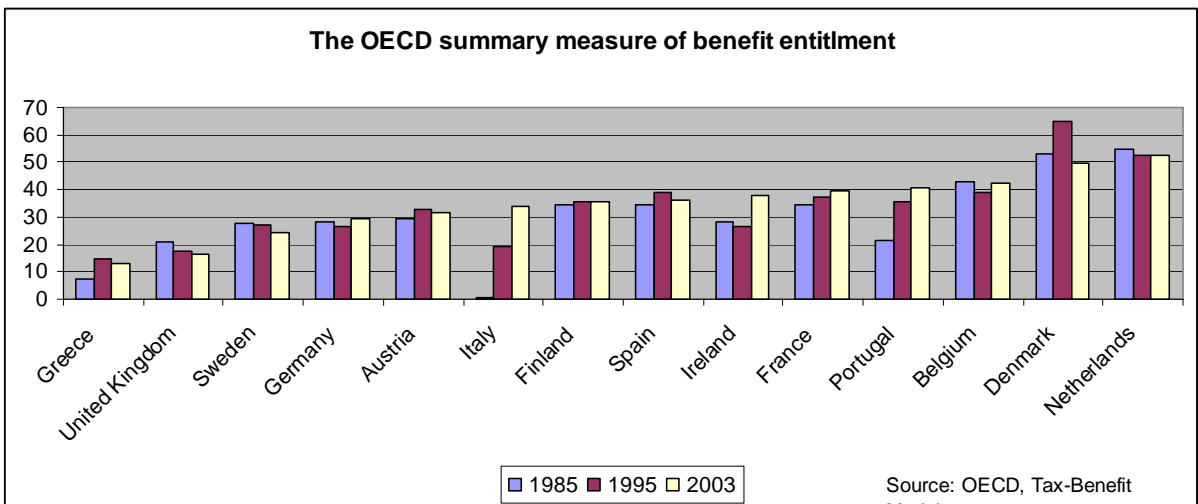


Having a special look at the dismissal law protection (on of five indicator of labour market regulation), Denmark and also Finland act different from their overall labour market regulation, while Germany acting as most regulated country in both considered perspectives.



One message could be: “Do not protect the jobs; protect the people by strengthening their life-long-employability.”

Unemployment benefits

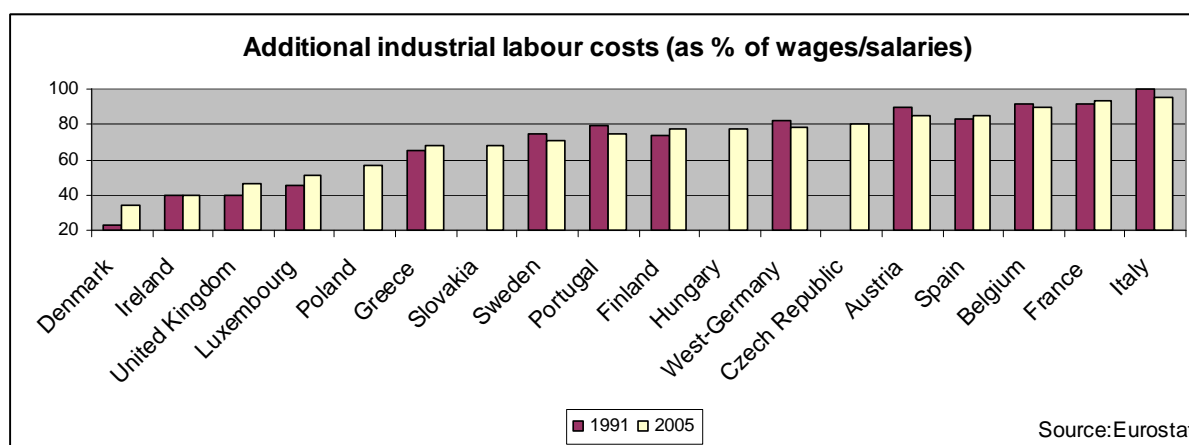


The OECD summary measure is defined as the average of the gross unemployment benefit replacement rates.³ It allows comparisons of the welfare benefits available to those in and out of work as well as the taxes they are liable to pay.

It shows up, that high benefit levels must not be linked with small employment rates and vice versa. Obviously, strong labour market activation with welfare-to-work programmes helps to realize a high level of social protection and high labour market participation.

Additional labour costs

Having a look at the different level of additional labour costs, we have to consider the following development. Continental European countries deal with the highest burden on employment. Therefore, Denmark and the Anglo-Saxon countries just follow a different strategy – which leads to better employment rates.



Further on, smaller additional labour costs are a stronger incentive to join the labour market, because net incomes are higher.

Enlist workers participation through profit sharing

Workers participation could be an important element of reconciliation of the labour force with globalisation. The participation of workers in profits of global economic development can thereby recreate trust in Europe’s institutions and free market economies.

In times of globalisation, that puts wages under pressure, and of demographic change, the way of strengthening the workers incomes by profit shares could help to stabilize incomes.

Accept immigration as a part of labour market policy

Low fertility will not resolve Europe’s unemployment problem. A more proactive and selective immigration policy could help to meet, not to overcome, this challenge. EU and its member states have to define their needs to go for brain gain and compensate for the brain drain (see contribution of Task Force 1).

³ Rates for two earnings levels, three family situations and three durations of unemployment. For further details, see OECD (1994), The OECD Jobs Study (chapter 8) and Martin J. (1996), “Measures of Replacement Rates for the Purpose of International Comparisons: A Note”, OECD Economic Studies, No. 26.

4.5 Complete the Single Market by reducing barriers/Service Directive

Reduce barriers of market entry (and exit), esp. the Service Directive

The single market is the motor of growth with more and better jobs. All measures that are taken to reduce barriers of freedom between the MS are welcome. Therefore, the Service Directive is a start but needs to go further. Exemptions (for example the social services) should be tested and renegotiated as soon as possible to help entrepreneurs to start their (often smaller) business abroad and test their market capacities with ease. The Service Directive does not aim to undermine social standards in the target countries, but to lift barriers of market entry abroad.

Reduce market regulations that harm functioning markets (European Social Funds/Globalization Fund)

All market regulations (labour markets, product markets, supply side, energy) that hinder the entry of new competitors or reward the correction of markets results should be treated with care (abolished).

For example on labour markets, it is the task of the private sector to create new and better jobs. So it should not be the task of the administration (legislation), strictly to hinder the disappearance of jobs. That does not mean to do without unemployment protection – but the protection should stress the goal of finding a new job and not to defend the previous job.

In this context, a European Fund to reduce the job consequences of globalisation has to be criticized. The better approach would be a preventive fund that would support the recovery process of the new MS and the MS still to come. Therefore, public money would be spent with higher rates of better overall competitiveness of Europe.

Strengthen SME-Policies by reducing bureaucracy

The initiative to force European wide the role of the SME with their special role as backbone of the economies and job motor is to underline. Especially the role of family steered firms should find support. Family owned SMEs are not only the backbone of the economy, but also of the social stabilities on the “ground” (in municipalities).

SMEs profit in a particular from lifting burdens of bureaucracy compared to big companies, because they often are not able to provide special knowledge (law, tax, statistical duties,). All initiatives to reduce the burdens of bureaucracy will improve the capacities of SMEs to focus on their success on markets and business.

4.6 Strengthen the Stability and Growth Pact/Reduce tax shifting without tax harmonisation

Ludwig Erhard, the former German chancellor said: “Sound money and low taxes are the best social policy!”

Therefore, the importance of sound public budgets should be underlined. Especially the burdens of former debt and upcoming expenditures for demographic change have to be provided. Despite these fiscal constraints, budget policies have to find ways to stress the importance of public education and formation for a Social Agenda of the future.

Tax harmonisation can not be the aim of European policies. National tax policies are a welcome instrument to adjust the public infrastructure prices to the needs of the inhabitants. In case, they require more and hopefully better public services and infrastructure, higher prices (taxes) are required. Nevertheless, companies should pay a minimum of their income taxes in the MS, in

which they make gains. Therefore, the approach of a appropriate harmonisation of tax bases and the simple non-bureaucratic distribution of the tax base between MS could be a helpful step, that takes in account the cross border activities of multinational firms.