What condition is Europe in? What constitution for Europe?

ZEI Conference sheds light beyond the German presidency

by Ludger Kühnhardt

In the first half of 1999, it is the turn of the German federal government to take over the presidency of the European Union. Heading the list of tasks to be tackled during this period is the decision on AGENDA 2000, the broad-based program of reforms being put forward by the European Commission. The intensity of current demands being placed both on the German presidency and the European Union as a whole must not, however, cause us to turn our attention away from the development of processes - now only slowly moving into the public eye - which will be of fundamental long-term significance for the EU.

Apart from the successful establishment of the euro, the key issue is that of pushing forward the process of creating a constitution for the EU, which will involve a long-sighted, sound reallocation of roles and responsibilities between regions or federal states, nations and the EU institutions. In the coalition agreement of October 1998, the parties of Germany’s new red-green federal government put the case for a European charter of civil rights which could indeed become an important stepping stone towards a European constitution.

MEDITERRANEAN POLICY

Along with eastern enlargement, intended as an expression of European security and prosperity, requirements for the coming years also include the development of a unified EU Mediterranean policy. This would mean that the Mediterranean region would come to be seen as the starting place in the search for shared security and prosperity for Europe, and would turn the southern countries bordering the Mediterranean into an object of strategic interest for the whole of the EU.

For this to succeed, the EU will have to reopen the Turkey dossier and attempt to remove the obstacle caused by Cyprus - still divided and ever further from a resolution of the ensuing problems - embarking on EU accession negotiations. Making headway on this is a vital pre-requisite to establishing a strategic, long-term community of interests with Turkey as the most important partner of the western world on the doorstep of the Middle East, the Caucasus and Central Asia. It is in Germany's own interests that Turkey be accepted as a "candidate country" and that its “European credentials” be measured strictly, but fairly, against the “Copenhagen criteria”.

TRANSATLANTIC ALLIANCE

1999 will see the completion of an advanced NATO strategy concept. The processes of reform in the EU and within the transatlantic alliance are not coordinated with each other, but they must produce complementary results and structures. In this context, the key requirement is that the EU and the USA as a learning community develop a common view of those challenges which must lead to consistency of objectives and complementary allocation of funds. This applies primarily to western policy vis-à-vis Russia, the Ukraine and Turkey. While there has been marked progress in developing a sustainable Euro-Atlantic partnership on global issues such as environmental protection and world trade, there has not yet been any real attempt to forge a strategic partnership to look at the consequences of the new geopolitical and geo-economic developments beyond the eastern and southern boundaries of the Euro-Atlantic structures.
INSTITUTIONAL REFORMS

As well as these far-reaching plans for ongoing development of a common foreign and security policy - which has been on the agenda for many years, but will certainly not be able to be driven forward sufficiently during a single presidency - the German presidency will provide the opportunity to discuss what improvements to the institutional structures of the European Union are necessary in order to create a more efficient, dynamic Union in the first years of the new century. The six-month rotating presidency gives all EU states a chance to present their European views within a federal partnership. At the same time, this puts a lot of organizational pressure on national government bureaucracies, and not just in the case of the smaller member states, whose resources are often insufficient to cope with the impact of a presidency. That is why we need to consider a new system of presidency for the EU that is as efficient and workable as it is federal.

The Amsterdam Treaty of 1997 left the matter of the majority principle as the guiding principle of decision-making in the EU essentially unresolved. Decisions on this have been put back until the next Intergovernmental Conference (in about 2002?). Since the admission of new member states will then have moved closer, the question of the priority tasks to be addressed, and will be required, during and beyond Germany’s six-month presidency, to balance their own, fundamentally held views with an appreciation of the requirements of a larger, strategic framework. Germany’s European policymakers will also be required, during and beyond Germany’s six-month presidency, to balance their own, firmly held views with an appreciation of the priority tasks to be addressed, and will be called on to reconcile the conditions for safeguarding the operationality of the EU with the requirements of a larger, strategic overall coherence. Maintaining continuity

A list of all ZEI-Publications which have been published so far is available on the Internet under http://www.zei.de.

The Publications can be ordered free of charge. Please call +49-228-73-9218 (Series B) or +49-228-73-1880 (Series C) or contact us by E-Mail: zei@uni-bonn.de.
in the established principles that have hitherto drawn cross-party support while continuing to expand Europe’s horizons is therefore an essential part of Germany’s European policy.

Against this background, the Center for European Integration Studies sees its contributions as a boost to the European debate in Germany and as a means of drawing together the different threads of European discussion. This became apparent at a ZEI specialist conference in January 1999 on the subject of “What condition is Europe in? What constitution for Europe?”. Leading academics and political experts took up the invitation of the Center for European Integration Studies to discuss the intellectual, legal and political implications of the issue and reflect on the long-term outlook.

In the run-up to Germany’s presidency of the EU, the ZEI provided an opportunity to look beyond the issues of the day and the laborious search for compromises on the issues currently under debate within the EU. The still distant goal of political union was brought back onto the centre stage again. Leo Tindemans, one of the great veterans of European politics and the former Christian Democrat President of Belgium, referred to the report from 1975 that bears his name in his opening speech. The occasion was to be a forum for the European public opinion hardly exists to-day.

Leading German political representatives at regional, national and European level (Minister of State Günter Verheugen, SPD/Member of Parliament, Foreign Office; Jo Leinen, SPD/Member of the European Committee of the regional parliament of Saarland; Prof. Dr. Hans-Gert Pöttering, CDU/Member of the European Parliament, President of the Europa-Union Germany; Siegbert Alber, Solicitor General at the European Court of the Europa-Union Germany; Siegbert Alber of the European Parliament, President Prof. Dr. Hans-Gert Pöttering, CDU/Member of the regional parliament of Saarland; Edward Bombhof (Nijenrode University, Netherlands), Manfred J.M. Neumann (University of Bonn), Alessandro Penati (University of Milano, Italy) and Jürgen von Hagen (ZEI and University of Bonn); Since the creation of the EMU Monitor two other groups have been founded with similar aims, one at the Centre for Economic Policy Research (CEPR) in London and the other at the Centre for European Policy Studies (CEPS) in Brussels.

**RECOMMENDATIONS**

The EMU Monitor has given its first press conference on 9 July 1998 at the Center for Financial Studies in Frankfurt. It recommends, for instance, a medium-term monetary strategy based on monetary targeting, which aims to keep inflation on average at a rate between 1% and 2%. Thus the group does not support the use of a direct inflation target. Important reasons for this choice are the problems connected with inflation forecasts and the lower informational input of monetary targets. Further, monetary targets are considered to be more transparent and more suited to build up reputation by the ECB during the early phase of EMU.

Since then, the ECB has decided upon a monetary strategy. The ECB strategy will primarily involve a monetary reference value, but it will also look at other economic and financial indicators when forming views about monetary policy actions. Clearly, the ECB has not taken up a strategy involving inflation targeting. The EMU Monitor considers the ECB strategy as very similar to monetary targeting, especially since the derivation of the reference value involves assumptions about trend growth rates of real GDP and the velocity of broad money, which are typically used to compute monetary targets.

At its second press conference on 17 December 1998 at the Frankfurter Presse-Club, the EMU Monitor has presented views on the economic outlook for the EMU area, monetary strategy, ECB accountability and the lender of last resort problem. In general, the EMU Monitor agrees with the ECB projections for the economic outlook of Euroland. Commenting on the co-ordinated cut in interest rates by the European central banks on December 3, the EMU Monitor thinks that this move was not based on economic grounds. It is rather seen as being motivated by the desire to reduce political pressure by the European governments on the ECB.

With respect to monetary strategy, the EMU Monitor believes that the reference value of 4.5% growth rate for harmonised broad money (M3H) is adequate. There is a risk that the trend rate of velocity becomes positive rather than negative, which would result in an expansion rate of M3H below 4.5% at given interest rates. In this case,
Prof. Dr. Jean Pisani-Ferry

Prof. Dr. Jean Pisani-Ferry is direct advisor of the French Minister of the Economy, Finance and Industry.

ZEI: What role does the Euro play in your opinion in the process of the European integration? Which further efforts have to be taken to make the Euro a successful project?

Pisani-Ferry: The Euro is both a powerful symbol of European integration and a very significant instrument for achieving price stability and growth in Europe. It will also enhance European integration, thereby fostering efficiency in the private sector, and, to an increasing extent, in the public sector also.

While the monetary constitution of the Euro zone has been laid down in great detail in the Maastricht treaty, more remains to do as regards economic and especially fiscal policy. The need for co-ordinating national economic policies is still a matter for debate among academics, but it is increasingly accepted among policymakers. No one really considers anymore that co-ordination would threaten the independence of the ECB. However, an efficient co-ordination requires appropriate procedures and institutions. Some rules are in place, and a new institution, the Euro-11, has recently been created, but my impression is that we are still in a learning process. In this context, there is a role for policy research in evaluating possible practical arrangements for organising co-ordination.

ZEI: Unemployment is a major problem in Europe. Which actions should be taken in the individual member states to improve the situation on the labour market? What do you think of the idea of an ‘employment pact’ on the European level?

Pisani-Ferry: Unemployment in Europe is both cyclical and structural. To the extent that it contributes to a better policy mix, co-ordination can help reducing cyclical unemployment. Structural unemployment is more of the responsibility of national governments, private firms and unions, but there is a role for European initiatives: first, a common commitment towards reducing unemployment can help focussing energies on that goal; second, structural policies to reduce unemployment have a trial-and-error nature. Some measures are successful, and some other are not. Furthermore, the delay between the decision and the actual results is frequently very long, which leads to blurr the assessment of the effectiveness of a particular measure. Confronting national experiences can help selecting the most efficient policies. This is after all a common practice in the private sector, under the name of benchmarking.

ZEI: The French-German Forum on Economic Policy was created to improve the understanding of Frech and German academics and senior policymakers about each other’s thoughts about economic policy. Do you see any important differences between the French and German understanding of economic policy which could lead to problems between the two partners of the European Monetary Union?

Pisani-Ferry: I could speak at length on this topic, but let me give you three short answers instead:
(i) there are obviously different economic policy cultures in Germany and France, but there is also increasing convergence. Just compare the situation today and ten or twenty years ago;
(ii) we should not aim at eliminating differences, but rather at clarifying what are the reasons behind our disagreements. This was the intention Jürgen von Hagen and I had when we created the Forum;
(iii) whatever differences we have, they are not such that they could represent a threat to EMU.

5th Political Dialogue in Maria Laach

In his introductory lecture at a ZEI colloquium in Maria Laach on the theme of “Germany and Europe - Positions, perceptions, prospects”, the Tübingen-based political scientist and spokesman for the European Centre for Federalism Research, Professor Rudolf Hrbek, outlined the problems and challenges for the German presidency of the EU in the first half of 1999. Le Figaro’s Germany correspondent, Jean-Paul Picaper, talked about the new phase in Franco-German relations following the change of government in Bonn, and the role of this partnership in the process of European integration. Developments within Europe made the question of a European constitution ever more pressing, the journalist explained.

The Finnish ambassador, Arto Mansala, whose country will be taking over the presidency in the second half of 1999, described the launch of the euro as the single European currency as a “victory of optimism”. It was now, he said, Germany’s responsibility to ensure the continued success of the single currency, and to push through the vital decisions on “Agenda 2000”.

ZEIreport No. 2 Feb. 1999
A Spanish and German Outlook on Europe - Agenda 2010

The distinguished speakers at this top-calibre academic political symposium in Madrid in late autumn 1998 cast their minds beyond the issues of the day to take a long-term look at the future of European development. The Instituto de Cuestiones Internacionales y Política Exterior (INCIPE), the editorial team of the prominent Spanish foreign affairs journal Política Exterior, the German Embassy in Madrid and the Center for European Integration Studies had jointly invited the speakers to Madrid for the symposium entitled “Agenda 2010: A Spanish and German Outlook on Europe”. The discussions by leading academics, journalists and politicians from both countries focused on the conclusions and implications for both countries - and for future progress in the European Union as a whole - of moving beyond the issue of immediate interest, AGENDA 2000. There were lively contributions by the Spanish crown prince Felipe and input from EU commissioner Marcelino Oreja, the Prime Minister of Catalonia, Jordi Pujol, the Mayor of Berlin, Eberhard Diepgen (Madrid and Berlin are twinned), the Chairman of the Committee of the Regions of the European Union, Professor Manfred Dammeier and others. The discussions made clear how essential it is to develop a common, coherent Mediterranean policy and to harmonise the strategic objective of eastern enlargement of the EU with the duty of solidarity within the European Union as it exists today. The findings of the workshop will be published in the ZEI’s own series of papers.

Seminar on International Trade, Labor Markets, and Integration

ZEI, in cooperation with Tartu University, Estonia, the University of Latvia, Vilnius University, and EuroFaculty, will host a week-long “Seminar on International Trade, Labor Markets, and Integration”. The seminar is funded by an EU PHARE grant and will take place at Tartu University.

SEMINAR STRUCTURE

The five days of the seminar are split into two sessions. The morning sessions consist of two presentations from senior staff of top Western European academic institutions in the three principle seminar areas. Each afternoon session consists of four presentations by young economists - eight from Western Europe and 12 from the Baltic States. Senior Western European participants are, Jürgen von Hagen (ZEI, University of Bonn), Torben Andersen (Aarhus University), Seppo Honkapohja (University of Helsinki), and Guiseppe Bertola (European University, Florence, to be confirmed).

SEMINAR TIMETABLE


Lithuanian President Valdas Adamkus at ZEI

Lithuanian President Valdas Adamkus is calling for Lithuania to be included at the earliest opportunity in the group of countries which the European Union has invited to embark on direct, focused accession negotiations. The head of state, speaking at ZEI in Bonn, explained that Lithuania had made considerable progress in bringing about reforms and was on the right path. He reminded his audience that the EU had recognised the stability of Lithuania’s democracy, the country’s commitment to protect civil rights and minorities, the strengthening of the legal system and the economic reforms of the last three years in its “Progress Report” published at the beginning of November 1998, which dealt with all 11 of the membership candidates. According to President Adamkus, the Commission’s criticism that progress in Lithuania was not yet sufficiently firmly grounded was based on out-of-date figures. His country wanted to join the EU, with all the rights and obligations that would entail, as soon as possible, he said. To ensure the necessary preparations are successfully completed, the momentum of reform has to be maintained by granting the country the clear prospect of accession within a specified timeframe. The Lithuanian president praised the healthy state of relations between his country and Poland and the normality of relations with Russia, whose internal crises also give cause for concern in Lithuania.

Junior Fellows Programme at ZEI

A “Junior Fellows Programme” for graduates, designed with young academics in mind and leading to a doctorate in political science, has been in place at the ZEI since the end of 1997. There are currently 14 Junior Fellows on this programme who are exploring a range of European topics as part of their doctorate projects. Research work centres on issues surrounding accession to the EU, Europe’s role in the world, the European institutions and their development, and the question of a European identity. The Junior Fellows usually meet every two weeks for a colloquium, in which they present their research projects and critically discuss the intermediate results of their studies.
news in brief

Prof. Christian Koenig is to take charge of the department of “Political, legal and institutional issues” at the Center for European Integration Studies (ZEI) at the University of Bonn from 1 April 1999. The legal specialist has until now held the Chair in European, National and Administrative Law at the Philipps University in Marburg. His research and teaching centres on European and telecommunications law. In addition, he has argued the case for linking community law with national commercial law in numerous publications, research papers and seminars. Koenig’s appointment means the last of the three head of department posts at the ZEI has now been filled. Koenig will bring a legal dimension to the work of the department, complementing the work of macroeconomist Jürgen von Hagen and political scientist Ludger Kühnhardt on the economic, political and cultural issues of European integration.

Dr. Aschot Manutscharjan joined ZEI’s Senior Fellow Program at the start of the year to begin his research project which will involve an up-to-date, in-depth analysis of the conflict between Georgia and Abkhazia.

A study entitled “Frankreich und das vereinte Deutschland. Interessen und Perzeptionen im Spannungsfeld” by Dr. Valérie Guérin-Sendelbach is to be published shortly by Leske+Budrich of Opladen. Dr. Guérin-Sendelbach, who previously headed “Workplace France” at the German Society for Foreign Affairs, joined the ZEI on 1 January 1999 as a new member of the research group “Institutions and development of institutions in Europe”.

Prof. Dr. Uwe Holtz will be based at the ZEI as a Senior Fellow from 1 April to 30 August 1999 while researching the subject of “50 years of European unity: the Council of Europe”.

Dr. Stefan Comes, a member of the “EU accession strategies” research group at the ZEI since 1 January 1999, gave a paper on “EU Enlargement and the Reform of the Common Agricultural Policy” on 21 January at the conference entitled “German and Polish Interests in the Eastern Enlargement of the EU” in Warsaw. The paper will be published shortly.

Prof. Kenneth Kletzer (University of California, Santa Cruz) will stay at our center in May and June 1999. He will work on EU-related issues of international macroeconomics and will play an active role in ZEI’s teaching activities on the post-graduate level.

ZEF has launched a new research program on Information and Communications Technology (ICT) and the Poor. The research is focused on the scope for lowering barriers and costs of access through appropriate institutional and organizational arrangements to facilitate participation of the poor in ICT. The project includes planned field work with colleagues from India, China, Peru, Bangladesh and Southern Africa.

ZEF organizes a ZEF Research Seminar and the Bonn Dialogue on Development Policy. The weekly ZEF Research Seminar is meant to promote the interdisciplinary discussion with external experts. Prof. Dr. Helmut Seitz (European University Viadrina, Frankfurt/Oder and ZEW, Mannheim) will visit Prof. von Hagen’s department (ZEI-b) from May through July 1999. His current research investigates the fiscal policy of subnational governments using the case of the German Länder.

Creating a joint European identity remains a central problem of European policy, according to the chairman of the CDU/CSU parliamentary group, Dr. Wolfgang Schäuble, speaking at the presentation of the book “Kontinent Europa. Kern, Übergänge, Grenzen” by Ludger Kühnhardt and Hans-Gert Pöttering at the ZEI. The CDU chairman admitted that the problems discussed in the book do indeed still pose an obstacle on the path to a wider, and simultaneously more integrated union. The issues in question are connected with “Agenda 2000” and European enlargement, as well as implementation of the principle of subsidiarity and democracy in the EU.


Dr. Wolfgang Schäuble on 2 December 1998 at ZEI

The Center for Development Research closely cooperates with the Center for European Integration Studies (ZEI). The two centers together constitute the International Academic Forum (IWB) at the University of Bonn. ZEF is an international, interdisciplinary research institute that contributes to resolving global development problems. Further information: http://www.zef.de

NEWS FROM THE CENTER FOR DEVELOPMENT RESEARCH (ZEF)

ZEF-WINDOW

ZEF-WINDOW

ZEF-WINDOW

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Household water insecurity is a pressing problem in developing countries. Unsustainable water withdrawal is increasing due to population growth, industrialization, urbanization, and increasing agricultural production which leads to various problems like water scarcity and insufficient water supply, especially in developing countries. In the framework of a multidisciplinary approach to the analysis of water problems, Prof. Patrick Webb and Maria Iskandarani elaborate in the ZEF discussion paper No.2 on water availability, access and usage, defining sectoral and cross-sectoral knowledge gaps. (P. Webb, M. Iskandarani: Water Insecurity and the Poor: Issues and Research Needs, ZEF Bonn, October 1998, pp. 66, ISSN: 1436-9931)

New research at ZEF emphasizes the importance of biotechnology for development. Martin Qaim and Prof. Joachim von Braun argue in the newly published ZEF discussion paper No. 3 that biotechnology can efficiently contribute to the achievement of development objectives. Policy-makers in developing countries and development organizations are challenged to select appropriate strategies for optimally harnessing the potentials of biotechnology for the poor. The paper presents a conceptual framework for ex-ante economic studies in developing countries. (M. Qaim, J. von Braun: Crop Biotechnology in Developing Countries: A Conceptual Framework for Ex Ante Economic Analyses, ZEF Bonn, November 1998, pp. 24, ISSN: 1436-9931)

The latest issue of ZEW-WINDOW is devoted to the theme of agricultural research and development policy. In a co-authored article, Dr. Bernd Schmid and Dr. Wolfgang Staudt discuss the impact of agricultural research and development policy in the former Soviet Union on the current food situation in that region and on the region’s potential to become a net exporter of food. The authors argue that agricultural research and development policies in the region have undergone rapid and significant change in recent years, leading to a shift from a planned economy to a market-oriented one. This change has had a profound impact on the food situation in the region and has implications for future policies.

In a separate article, Dr. Martin Kramarz and Dr. Ulrich Weidenfeld examine the role of agricultural research and development policy in the former Soviet Union in promoting economic growth and development. They argue that agricultural research and development policies have played a crucial role in promoting economic growth and development in the region, and that future policies should continue to focus on promoting innovation and productivity in the agricultural sector.

In addition, the latest issue of ZEW-WINDOW includes a discussion of the impact of agricultural research and development policy in the former Soviet Union on the region’s potential to become a net exporter of food. The authors argue that agricultural research and development policies in the region have undergone rapid and significant change in recent years, leading to a shift from a planned economy to a market-oriented one. This change has had a profound impact on the food situation in the region and has implications for future policies.

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Can more flexible labour markets in Europe lead to less unemployment? A new ZEI study contributes to this debate

by Robert MacCulloch

When European leaders met in Copenhagen in June 1993 they were given a special presentation on the problem of unemployment in Europe by Jacques Delors, President of the EC. Delors explained that a lack of competitiveness with the United States and Japan was the basic cause of the rise in unemployment, and that a program of investment in infrastructure and high technology would be the cure.

His speech disappointed Paul Krugman, Professor of Economics at the Massachusetts Institute of Technology. Krugman’s understanding was that economists who studied the European situation mostly shared “more or less the same diagnosis of the European problem: the taxes and regulations imposed by Europe’s elaborate welfare states have made employers reluctant to create new jobs, while the relatively generous level of unemployment benefits has made workers unwilling to accept the kinds of low-wage jobs that help keep unemployment relatively low in the United States.”

Economists advising countries on these issues have been concerned, in particular, about the adverse effects of regulations relating to hiring and firing restrictions faced by firms. A number of countries have taken their view seriously. Great Britain and France are just two examples of countries that followed the economists’ advice and reduced hiring and firing restrictions in the mid-1980’s to combat high unemployment. This view of the labour market has also inspired large reform programs in the less developed world, where unemployment has recently increased. In fact, deregulation of the labour market is part of what the Washington Consensus often calls “second generation reforms”. Labor flexibility is one of the main features of the IMF’s recent agreement with Argentina, where unemployment reached an alarming 18.6% after the first 5 years of reform.

Since unemployment brings real misery to people’s lives, and job security provisions often involve delicate redistribution issues between richer firm owners and poorer workers, the economists’ advice is potentially politically explosive. One would think that economists giving such advice know what they are doing. More precisely, one would think that there are hundreds of papers studying whether more flexibility in fact does reduce a country’s unemployment rate in practice. Sadly, this is not the case. To our knowledge, there is one panel study on the effects of labor market flexibility, and only a couple of cross-country studies, like that in the OECD Jobs Study (1994) based on 21 observations. Two leading U.K. economists, Gregg and Manning, review some of the available evidence on the effects of labor market flexibility and argue that it is “much less persuasive than is commonly believed”, and that the profession’s “faith in the merits of labor market de-regulation is misplaced”.

RECENT RESEARCH ON FLEXIBILITY AT ZEI

In the paper, “The Consequences of Labour Market Flexibility: Panel Evidence Based on Survey Data”, joint with Rafael Di Tella of Harvard University, we make an empirical contribution to this debate. We introduce a new panel data set on labor market flexibility from the World Competitiveness Report, which is based on surveys of business people in 21 OECD countries during 1984-90, so the indices we use are subjective in nature. One of the virtues of the data are that it originates from people who have to make their living out of roughly understanding how stringent job security provisions actually are in their countries.

The use of a subjective index allows respondents to capture movements in very different kinds of regulations that affect the flexibility of labor markets. These may include regulations on an employer’s freedom to dismiss workers (which depends on severance payments, requirements of advance notice and authorisation by third parties - such as a trade union - as well as provisions for appeal against unfair dismissal), the enforcement of these rules, interpretation of what constitutes legal cause for termination, limits on the use (or the legal validity) of fixed-term contracts, limits on the use of temporary work agencies, limits on employer’s use of part-time work, and so on. These regulations imply very different costs to normal business operations and would be extremely difficult to document with hard data.

There are, of course, limitations to the subjective data that we use. The index is more vague than what an economist would ideally like to use. By its nature, our flexibility index does not allow us to distinguish between the effect of the different regulations that are active. However, we believe the relevance of the subject matter and the
evidence available to the profession to be so out of balance that a willingness to experiment with survey data is justified. We then present an empirical analysis of the effect of flexibility on a number of labor market variables.

**WHAT DOES THE EVIDENCE TELL US?**

We find that countries with more flexible labor markets have higher employment rates and higher rates of participation in the labor force. We also find some evidence of a positive effect of flexibility on the number of hours worked per week. The estimated employment effects seem to be large. A conservative estimate is as follows: if Germany were to increase the flexibility of its labor markets to US levels, the employment rate would increase by 1.7 percentage points, almost 24% of the actual difference in employment rates between the two countries.

In terms of income, this employment gain could bring about a 2.7% increase in German GDP per capita. Of course, this says nothing about the convenience of such a reform. For that we would need information on the benefits (in terms of employment security, wages and so on) of flexibility, a fact sometimes forgotten in policy debates.

The paper only finds some evidence that countries with more flexible labor markets have lower unemployment rates and a lower proportion of long term unemployed. The Figure above shows the relationship in the pooled data set between unemployment (on the vertical axis) and flexibility (on the horizontal axis), in which there appears to be some indication of a negative relationship.

We also find evidence suggesting that recessions are associated with higher inflow rates into unemployment in more flexible labor markets (this is as close as we can get with the data available to testing the hypothesis that regulation interferes with job destruction). Lastly, we explore some alternative hypotheses related to flexibility that have been suggested in the literature. First, we examine the jobless recovery hypothesis and find evidence which suggests that GDP growth is associated with smaller reductions in unemployment in countries with very inflexible labor markets. We also find that unemployment is more persistent in countries with more inflexible labor markets.

**FUTURE WORK**

To further our understanding of the issues surrounding labour market flexibility, ZEI is about to embark on a Workshop program jointly with the new Institute “Zukunft der Arbeit”, to bring together a group of prominent researchers in this field who will present and debate their latest findings. There are many unresolved issues in theory, evidence and policy which need to be addressed. Theory problems include better definitions of the word “flexibility”, which has been used not only to refer to the size of hiring and firing costs, but also to regulations on qualification, regulations concerning the work place, quotas for women and handicapped persons, and so forth. Significantly more econometric evidence is needed on the labour market effects of flexibility. Policy questions include the appropriate-ness of increased flexibility as a means of reducing European unemployment. Should European labour markets be subject to greater deregulation?

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