

The European Employment Strategy: Policy Integration by the Back-Door?

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Abstract

Since the signing of the Maastricht Treaty, the EU has paid increasing attention to employment creation, yet has few formal powers in this area. A series of agreements, known as ‘processes’ and named after the city where they were agreed, has been made to co-ordinate employment policy. This paper will explain how the ‘Luxembourg process’, under which member states structure their employment policies, works and will offer a critique of the ‘open co-ordination’ approach to employment policy. The focus will then shift to the extent to which the OMC represents simply a first stage in the eventual communitisation of policy or new method in its own right. It will also confront the question of whether this form of policy can be expected to go far enough to constitute a sufficiently robust ‘real’ economy counterpart to monetary union.

Introduction

Switching from national currencies to the euro is much more than the replacement of notes and coins or the transfer of responsibility for monetary policy to a new supranational body in the form of the European Central Bank (ECB). It is bound to transform the manner in which economic policy is conducted and, because it alters the scope for different policy instruments to act, to require a recasting of the policy framework. Some of the elements of this new framework are now firmly established, while others are still being pieced together (Hodson and Maher, 2000).

The architecture of demand-side policies under EMU is clear. Monetary policy is assigned the primary task of assuring price stability, leaving fiscal policy – which remains under the jurisdiction of national governments – to deal with country-specific macroeconomic problems. The latter, however, is constrained by the *Stability and Growth Pact* (SGP), which means that if a country has to deal with more severe economic shocks, it may be unable to do so under the terms of the Pact (Eichengreen and Wyplosz, 1988). The Pact, moreover, has an in-built asymmetry in that it sets limits to national deficits, but imposes no rules on public surpluses. There is, therefore, a co-ordination issue to resolve if the aggregate fiscal policy of the Euro-zone is to be consistent with monetary policy (Leith and Wren-Lewis, 2000). Gradually, the institutional machinery to achieve this has been put in place through measures such as the Broad Economic Policy Guidelines – agreed annually between the European Commission and the Council - and the establishment under the so-called ‘Cologne Process’ for macroeconomic dialogue. It is open to question, however, whether this goes far enough (see, for example, Jacquet and Pisani-Ferry, 2001).

Artis and Buti (2000) argue convincingly that for a variety of reasons, it will make sense for Member States to aim for a fiscal policy ‘close to balance’ over the medium-term. As this dovetails with the rules of the SGP, the inference to draw is that fiscal policy can only play a limited role in economic adjustment. With the exchange rate no longer available, it follows that countries need to rethink the use of other policy instruments to deal with shocks of various kinds. The principal options fall under the loose heading of supply-side policy, to some extent, the European Employment Strategy (EES) can be seen as creating one such mechanism.

Reform of employment and social welfare policy is high on the agenda in most Members States, for other reasons as well. Concerns about competitiveness, unemployment and the threat from future pension liabilities are powerful drivers for reform. Although the threats to the European social model are frequently over-stated (see Ferrera et al, 2000), there is a manifest need for reform of the welfare state. Because of the sensitivity of national accommodations in social policy, harmonisation is clearly not an option, but it is an area of policy in which there are evident differences in philosophies and structures.

One of the requirements for the development of European policy is agreement on objectives and the means to achieve those objectives. So the first section of the paper examines the case for European employment policy. The emerging policy framework of the Open Method of Co-ordination (OMC) particularly as applied in the EES will then be analysed. The third section of the paper will consider the advantages and disadvantages of the methods of integration employed. The impact of the OMC as embodied in the EES is then evaluated. The nature of the OMC as a policy regime, i.e. whether it is a new policy method or whether it represents merely an intermediate stage to eventual communitarisation is the subject of the final section.

Why Consider Europeanising?

As EMU is consolidated, it is likely that a need will, for a variety of reasons, arise for at least some integration of employment policy. Widely divergent arrangements may not be consistent with the single market, especially if they systematically affect operating costs of business. Social expenditure, averaging 28% of GDP in the EU, plays a significant role in assuring macroeconomic stabilisation, but the impact is largely within national boundaries rather than cross-border. More generally, the recasting of the policy framework consequent upon the move to EMU invites fresh thinking on these issues (Crouch, 2000).

The advent of monetary union reinforces the case for the EU level to play a more extensive role in employment policy, particularly in developing an over-arching framework within which local actors can deal with employment problems. It might, however, be asked why Europeanisation of employment policy should be contemplated, given that national traditions and priorities are so diverse. Certainly, although there have been extensive changes in employment and welfare policy there does not seem to be any clear tendency towards convergence (Boeri, 2001), but it can be argued that shared values - such as a commitment to 'minimum guaranteed resources' - justify greater EU involvement. Moreover, various justifications for doing so can be put forward.

There are manifestly common problems. Despite the recent decline in the headline total of unemployment, all Member States bar Luxembourg have pockets of persistent unemployment, a significant proportion of which result from EU-wide structural changes. Thus, although there is clear national diversity in forms of employment problems, it is clear that it is something that European society as a whole has to face.

The deepening of European integration could itself justify a rethinking of the assignment of policy competencies. There are arguments suggesting that the need for employment policy lessens with the degree of integration if for example local shocks are buffered by more extensive market interaction. Thus the elimination of exchange rate variability may diminish fluctuations in the demand for labour. Financial market integration can make it possible to reduce local risk as a result of portfolio diversification and cross-border credit. Estimates suggest that this is the most important means of cushioning regional specific shocks in the USA (Asdrubali et al, 1996; Melitz and Zumer, 1999). Market integration, particularly financial market integration, is far from complete in the EU, so this mechanism is largely absent in EMU. In addition although EMU reduces exchange rate instability¹, merely shifts the locus of adjustment to country specific shocks.

With increasingly free mobility of goods, capital and labour in the single market and EMU makes it easier for economic actors to avoid legal restrictions. Thus there is a fear that the tax base necessary to finance national social security and employment assistance will be undermined by mobility of labour and capital. The most heavily taxed factors capital and skilled labour also tend to be the most mobile, thus potentially limiting national policies.

Deeper economic integration will in addition mean that market failures whose correction requires collective action and enforcement, will pose problems where the collective action and enforcement are national but the markets are European. Thus whilst labour mobility is seen as a desirable adjustment mechanism in EMU (Obstfeld and Peri, 1998), migration implies a greater elasticity of labour supply causing problems for independent employment policies. Thus a country that imposes high labour taxes will find that this leads to migration and lower revenues. For example generous unemployment benefits in Germany provided an effective floor below which wages would not fall, that was lower than the wage workers from other countries such as the UK and Portugal would accept. This encouraged an influx of foreign workers to be employed in German construction industry leading to unemployment among German construction workers. This problem was resolved by reducing German unemployment benefit and introducing a minimum wage for all workers employed in the German construction industry. This effective minimum import price was exempted from single market rules. Thus the Single Market undermined policies designed to protect construction workers from the cyclical nature of their industry (Bean et al, 1998).

EC legislation can also directly weaken national law-making and enforcement in the employment field. Thus the prohibition under the Treaties of discrimination on a national basis places limits on national welfare systems. The principle of non-discrimination may be difficult to reconcile with the redistribution that is at the heart of these systems. These problems are compounded by the provisions of the Stability and Growth Pact, which whilst only directly restricting public sector deficits has potential effects on social welfare systems, especially when combined with population ageing. Thus the 3% deficit limit may be difficult to reconcile with relatively generous social security provisions, during an economic downturn

as unemployment increased payments would rise and revenue would fall, potentially driving the deficit beyond the 3% limit. Deficit limits may also make it hard to agree difficult welfare reforms, for example pension reform, because the finance is not available to smooth the path of adjustment.

Differences in social security systems can also present problems for the efficient operation of EMU. The very large variation in the level of benefits between countries raised the possibility of 'vacationing' by the unemployed, moving to countries where unemployment was higher. To limit this possibility the duration of unemployment benefit is a maximum of three months if the unemployed moves away from the country where the job is lost (European Commission, 1997). Since national unemployment benefit typically lasts longer than 3 months this acts as a deterrent to the international mobility of the unemployed.

The need to avoid distortion of competition in the Single Market also place limitations on national employment policy. For example the Commission ruling against Italy's subsidisation of new employment by "contratti di Formazione e Lavoro" (training employment contracts), which were seen to benefit employers (rather than workers) (Jimeno et al, 2001; p.88).

The step increase in economic integration implied by EMU thus provides a strong case for further Europeanisation of employment policy. The fundamental problem was how to develop European policy in an area where national differences in policy and approach were so great? The limits of the Community method are clearly shown in the Social Agreement reached at Maastricht. Here the less controversial areas largely deriving from earlier Treaty commitments such as equal opportunities, the health and safety of workers and workers and equal pay between men and women are subject to QMV. But new more controversial areas including social security and employment protection require unanimity. With Europe's unemployment problem and the new challenges of EMU a new approach was needed and this was provided by the OMC.

The emerging policy framework

The European Employment Strategy

Since the Essen European Council in 1994, the EES has gradually evolved, receiving a significant boost from the inclusion of an Employment Chapter in the Amsterdam Treaty. This led directly to the agreement, in December 1997, on what is now known as the Luxembourg process, an annual cycle for elaborating, implementing and monitoring national employment policies. The key to this process is the Employment Guidelines a decision of the Council based on a proposal from the Commission. These provide the foundation upon which each Member State draws up a National Action Plan (NAP) describing how these Guidelines are to be put into practice in the way judged to be best suited to that country. This process should involve a wide range of partners: unions, employers, local and regional authorities, etc.

The EU employment guidelines

The employment strategy is encapsulated in the guidelines, which serve as a template for the development of the NAPs. These guidelines evolve from year to year in response to changing economic circumstances and decisions taken at the European Council. Following the March 2000 Lisbon European Council, Member states were asked, for example, to develop policies to raise the aggregate employment rate² and to support the transition to a 'knowledge-based society'. The 2001 guidelines (Council, 2001) have 19 clauses that cover the four pillars of policy, with a series of objectives under each. The four pillars are:

- *Employability*, which is about supporting workers to gain initial employment, maintain employment and obtain new jobs, with particular emphasis given to lifelong learning and preventative measures. Specific guidelines cover areas such as action to reduce youth and long-term unemployment, and to provide pathways into employment.
- *Entrepreneurship* concerns the ease with which a new business can be started and enabled to employ people. Because of the higher potential for employment in many service industries, governments are asked to focus particularly on these industries.

- *Adaptability* is about developing more flexible ways of working and of organising work, so that firms can be more competitive and responsive to demand. As part of this, plans are expected to put forward proposals for improved training.
- *Equal opportunities* refers to measures to make it easier for women, especially, to obtain access to jobs and training, as well as equal treatment at work. This last group of guidelines is advocated, in part, to maintain the essence of the European social model. The French emphasis on rights is, clearly, prominent in this respect, but so too are many of the Nordic traditions.

In addition, the Member States have to take into account issues such as the development of the information society, the need to bring undeclared work into the open, and the promotion of local and social employment. As part of the procedure, quantitative targets and indicators have to be developed, while a key expectation is that EU resources such as the Structural Funds should support the European Employment Strategy.

Key points to note about the Luxembourg process are that

- Member States of the EU are expected, in their NAPs, to indicate how they plan to make progress on the four pillars of the employment strategy. These are then subject to scrutiny both by the Commission and, in the Council, by other Member States.
- This ‘peer review’ and ‘peer pressure’ could be said to improve the prospects for policy co-ordination and might assist the search for gains in policy efficiency.
- It also draws attention to governments that do not achieve much by exposing them to scrutiny and the prospect of being given an adverse rating in ‘league tables’.
- The pressures to adopt common statistical tools and to use benchmarking could help to improve national monitoring and adaptation of policy.
- The EES does not include sanctions against states that do not conform to the guidelines or achieve what they say and has no financial resources at its disposal, prompting the question of whether it can hope to achieve much impact. Its potential impact is, therefore, likely to be qualitative in nature and its focus on improving national policy-making by means of a common framework and processes.
- There is a potential for confusion about where ultimate responsibility for job creation lies and this could both weaken the coherence of the EES and call the legitimacy of the policy into question.
- While the Commission has an important role, it is more technocratic and enabling than strategic.

The National Action Plans (NAPs) are central to the EES, they are the mechanism by which Union aspirations can be translated into national policy. They can be seen as tools of policy integration (Begg, 1999; Madsen, 1999) promoting integration between policy in different Member States and between labour market policy and other policy areas. The NAPs are also part of a political process where different actors try to influence the national and EU agenda and policy (Goetschy, 1999; Jacobsson, 1999; Jensen, 2000; Teague, 1999). Thus national Ministries of Labour, and the social partners more generally have shown a great interest in this process (Johansson, 1999)

Member States’ National Action Plans can, to some extent, be clustered along geographical and functional lines (Madsen and Munch-Madsen, 2001). Thus, there is a North-South split and, within the former group, evidence of regimes which focus on curbing unemployment as distinct from those with wider ‘corporatist’ ambitions, showing that substantial variations in approach can be accommodated. Much of the difficulty in agreeing any supranational policy in the area of employment policy derives from the breadth of the areas potentially involved (e.g. employment protection legislation, social welfare and security), their sensitivity and the disparate national traditions that underpin policy. For example in welfare³ the differences between the Bismarckian social insurance approach, the Nordic emphasis on active labour market policy or the safety net of the Beveridge universal approach. One of the virtues of the OMC is that it is sufficiently flexible to accommodate these national differences.

Methods of Integration

The OMC and Employment Policy

OMC's principal advantages are that it provides the means to move towards common solutions to common problems without demanding the sort of harmonisation that would be anathema to many governments, and that it can be implemented by governments without recourse to major and potentially contested legislative change. Moreover, by allowing countries to shape national programmes within common guidelines, OMC allows governments to weight their policy packages appropriately. Such *differentiated policy harmonisation* would represent an artful compromise between policy integration and subsidiarity. Politically, the mere fact of being seen to 'do something' is likely to be appealing to governments. The question that then arises is whether this outcome is one, which goes far enough to resolve problems common to all Member States.

The potential drawbacks of OMC can be grouped under four headings. The legitimacy of OMC is dubious. This is despite the fact that the intimate involvement of national government in the process seems to invest the process with the legitimacy of the national state. This it can be argued is little more than a veneer, the OMC does not answer the fundamental criticisms of EU governance: elitism and opacity (Hodson and Maher, 2001). The democratic legitimacy of guidelines drawn up by unaccountable officials and agreed by representatives of national government in closed session is questionable. Especially in so politically sensitive a policy area, however well intentioned the proposals and the underlying diagnoses. Decisions in areas like employment have always been reached through a delicate process of mediation between national interests, so that if guidelines are issued by 'Brussels' that call for unpopular or controversial reforms they risk being seen as unacceptable (Chassard, 2001). A risk in this regard is that the EU could be used as a scapegoat. Indeed it might be argued that this could provide part of the motivation for Europeanisation, thus governments could try to push through unpopular measures such as pension reforms at the European level in order to circumvent a lack of domestic support⁴.

Second, there is the issue of monitoring and enforcement of policy. Here, there is a tension at the heart of OMC. The more strictly any targets are monitored, the less the discretion available to a Member State in shaping programmes. At the same time, if there is no sanction (or, as was the case for the EMU convergence criteria, a reward) for failing to adopt suitable measures, let alone meeting targets, the attempt to co-ordinate could prove to be empty. Third, the degree to which the OMC genuinely leads to policy innovation rather than repackaging of existing policies is germane. In the EES, the evidence from the first three annual cycles is that policies have evolved and that governments have learned from their counterparts.

The fourth drawback is that the OMC could be used as a pretext for avoiding hard decisions about the appropriate recasting of policy competencies in the EU policy framework, bearing in mind the salience of the integration of monetary policy.

Target or Benchmarks

One of the more vexed questions about OMC is how to set and monitor targets and there are various ways in which this can be done. However, it is far from obvious how any target should be devised, monitored and enforced. With the Maastricht criteria, the 'prize' for conformity was accession to the first wave of EMU. Although there are some possible carrots available, such as discretionary EU spending, the likelihood that the European Council would agree to these being used to reward success in achieving employment policy targets is remote. But even if targets are only advisory, they could still have a potent effect by exposing governments that fail to achieve them to criticism from their electorates and it may be that the experience of the NAPs will play a part.

Benchmarking could allow the outcomes of employment policy in one country to be assessed relative to other countries. One of the great attractions of benchmarking is that when 'league tables' are compiled, no company or country will want to find itself at the wrong end of the table and thus be shown in an ostensibly objective manner to be deficient. The threat of being exposed as having slipped from an acceptable position

exerts a discipline on those responsible for performance and will oblige them to focus on the consequences of what might otherwise be 'soft' decisions.

Using benchmarking as the basis for 'rewards', as with the Maastricht convergence criteria, could lead to a separate difficulty, namely that success in meeting one set of criteria may be achieved *at the expense* of missing others. A company can raise its profitability in the short-term by reducing its spending on R&D or marketing, but such cuts would be expected to undermine its long-term competitive position and compromise future sales. Similarly, with employment, a tougher stance on workfare might lead to marginal groups simply 'disappearing' from the labour market altogether.

The OMC and the development of employment policy

Examples of areas where the OMC has helped to enhance employment policy in individual Member States include the following:

- Integration of policy across different areas of responsibility. Active labour market policy may make sense in its own right, but is likely to have a greater impact on employment if it is embedded in a broader policy setting. Member States are bound to vary in the mix of policies they have put together and could gain from exposure to a wider set of approaches.
- The institutional make-up of the policy system and the degree to which various interests are involved. The social partners plainly play a big role in Denmark as and have assisted in the reform in the Netherlands. But, the social partners may tend to represent their members and supporters more readily than wider societal interests.
- How other non-governmental interests, such as voluntary organisations, are involved is also important. They can influence policy in two distinct ways: as advocates of change by representing particular constituencies in the policy debate (Ireland is a good example of this); and by developing new functions in the delivery of policy that complement what is provided by public agencies.

Welfare systems, plainly, need to adapt to new demands on them, while continuing to fulfil their role in attenuating inequality. Modernised and productive social protection also has to be seen as part of the *economic* policy framework under EMU, as well as having social objectives. It is for this reason that a fresh look at how incentives operate in welfare systems is proposed as one of the guidelines. The advantage of OMC in this regard is that there is scope for countries not only to learn from one another, but also to exploit the benchmarking process to reveal weaknesses and potential for enhancement of policy delivery.

Innovation in employment policy, comes not just from government action, but also from the involvement of other social actors. The contributions of the social partners and voluntary groups, in particular, can be enhanced by developing new approaches. The degree to which local agencies are empowered and motivated will also be vital. Again, the diverse national approaches ought to be a source of strength: for instance, the success of the Netherlands or Ireland in engaging the social partners (indeed, a broader partnership in Ireland) offers lessons for others.

A formal evaluation of the effect of the EES on Member States employment policies is difficult because of the comparatively short period over which it has operated, combined with the lags before the effects of supply side measures are felt. The policy effectively began operating in 1998 so only three annual reports on employment policy have been published (European Commission, 1998, 1999, 2000). "An overall impact of the European Employment Strategy on the improving employment situation is difficult to identify. Most recent data refer to 1999, the year in which most policy reforms started to be implemented under the NAPs." (European Commission, 2000; Section 2). There are, however, some observations that can be made about the operation of the system. Given the great heterogeneity of EU countries, both in their employment situation and in their employment and social welfare policies. Thus the employment rate exceeds 70% in Denmark, Sweden, the Netherlands and the UK but is below 55% in Spain, Italy and Greece (European Commission, 2000). Second this heterogeneity carries over into the response to the guidelines, thus there is convergence of policy in some areas but not in others. In the case of the guideline of employability Member

States generally redirected expenditure for the unemployed from passive⁵ to active measures (e.g. training) over the period 1985-99. But over the period when the EES came into play there is little evidence of further redirection from passive to active despite the this being one of the guidelines (Madsen et al, 2001). Thus the overall effect of the EES on Member States employment policies is unclear at the moment.

Policy integration by the back door?

The OMC in general and its particular manifestation in the European Employment Strategy could be seen as simply a stage in the process of full communitisation of this policy area. Thus the establishment of the Strategy, its guidelines, identification of best practice, benchmarking, peer review and recommendations should lead to a convergence of policy. The extensive engagement of government ministers and civil servants in the process will also produce a convergence of the ideological underpinnings of the policy, which will in turn reinforce the convergence of policy. This increasing convergence will highlight the problems associated with the lack of a common policy. When sufficient convergence of policy and ideology is achieved and the advantages of a full EU policy increasingly appreciated, the elites involved in the process will initiate the process of developing new EC legislation and of legitimating EU policy in the Member States. Although superficially this might seem to be the direction the EES is taking, the reality is more complex.

The problems in the communitisation of the EES can be illustrated by a comparison with EMU the area of economic policy that has mostly recently undergone this process. EMU began with cooperation among Member States in the European Monetary System, which to begin with lacked formal Treaty backing. The members of the Exchange Rate Mechanism increasingly perceived the benefits of the system and exchange rate stability improved, further enhancing the benefits of the system. Gradually problems with the operation of the particular system, in particular the effects of German hegemony, began to be perceived. Monetary union was increasingly seen as the means to resolve these problems and to produce significant benefits, as well as to advance the cause of European integration. At the same time the political elites view of the economic world was shifting⁶ the prevailing ideology shifted from the benefits of interventionist economic policies to the benefits competition in markets, of sound money and sound public finances. Thus the mid-1980s saw the launch of the Single Market and the culmination and completion of which was to be the Single Currency (Emerson et al, 1991). The shift to monetarism also provided a means to achieve European monetary union without the simultaneous development of a significant European economic government as proposed in the original blueprint the Werner Report (Werner et al, 1970). This was important because Member States had always been reluctant to pool sovereignty in the sensitive areas of taxation and government expenditure. Thus Maastricht model of EMU involved supranational governance of monetary policy, where sovereignty had already been limited by the EMS and the independence of national central banks. In economic policy national public deficits were to be limited in line with the developing orthodoxy on sound public finances but beyond this economic policy was to be subject to the open method of co-ordination. Thus EMU could be regarded the ultimate achievement of what Tinbergen termed negative integration.

It is difficult to see a similar pattern of development for the EES. The process of monetary integration began with the simplicity of the ERM/EMS whereas the EES is notable by its complexity. This complexity is the result of the profound difference in employment policies that have their roots in different histories and ideologies and are intimately related to the society in which they exist (Esping-Anderson, 2001). Thus employment policy combines inputs from the state, the market and the family. Thus part of the difference between Northern and Southern Europe in this area is the result of familialistic nature of the Southern welfare systems. This explains why youth unemployment remains so high in Southern Europe in the absence of social entitlements, young people live at home and require a wage and security in employment sufficient for them to live independently. Seen in this wider context the imperatives for Europeanisation do not seem as persuasive. Whilst millionaire German and British motor racing drivers may choose to reside in Monte Carlo, they have freedom of location with regard to their employment and are rich enough to be able to afford the private services they need. Although there may be some cross-border opportunism free riding on superior health systems, this is not usual. Generally lower taxes are the corollary of lower social benefits,

poorer health and education services. Welfare spending and GDP are also strongly correlated (Bertola et al, 2001; p.31). Thus the pressure from migration on the tax system is likely to be muted.

Similarly the potential to exploit differences in welfare systems by migration are limited. First by the criteria to determine entitlement, which generally require residence and/or tax contributions and in their absence severely limit benefits. Second differences in prices offset a substantial amount of the difference in welfare levels. Third the problems of language, culture and family ties act as a substantial brake on migration. Such factors are likely to be more important for migrants dependent upon benefits than those working because their social exclusion would be substantially increased by migration.

It could of course be companies rather than individuals that migrate from high cost/taxation locations to areas where wages and taxes are lower. Industries where wage cost differences are central are likely to be migrating most likely to locations where wage costs are so much lower taxation is irrelevant. Given the high level of costs in the EU competitiveness is only possible through productivity and quality. Here the greater commitment of a workforce based on general social solidarity in engendering competitive advantage than greater incentives to work brought about by lower taxes and social benefits.

Many recent contributions to the debate employment policy have emphasised the need to modernise and reform social protection (Bertola et al, 2001). The role of social protection as a productive factor has been especially stressed, with other areas for attention including pensions reform. The scope for social protection to act as a productive factor, in the sense of contributing to the better functioning of the economy and improved productivity growth, is thought to be considerable. This focus is not without its opponents, who object to the watering-down of the 'solidarity' element of the social model and see this as incompatible with the political aims of social policy. However, it is clear that this is a dimension of policy that cannot be ignored in the present climate.

Thus social protection can provide flexibility in the labour market. It does this by providing a guarantee of income that facilitates movement between jobs. Individuals are able to engage in a more extensive job search and thus, in principle, to assure a better match between their labour market attributes and job specifications. With pervasive unemployment, the efficacy of this may be diminished, although the challenge to policy-makers is to design systems to accentuate the positive role.

Social protection may in addition provide insurance against adversity in a way that influences the long-term productivity of labour: prevention, in this context, is better than cure. Indeed, it can be argued that measures, which support productivity enhancement, contribute to, rather than detract from, economic growth. Publicly-funded health care, and provision for sickness and invalidity fulfil this function by contributing to the well-being of the labour force. In this regard it is worth noting how many American employers provide health insurance as part of the remuneration package. Their motivation for doing so is not hard to guess and it is reinforced by tax breaks. Another function of social protection that has been especially emphasised in the debate triggered by the Commission Communication is in reintegrating the socially excluded. Social protection can do this by providing pathways back into employment for marginalised workers and by making it possible to upgrade the skills of, or retrain, vulnerable workers.

The history of the European welfare state shows that social protection serves first and foremost to secure social cohesion and stability in society (Swaan, 1988). In the founding treaty of the European Union this seems to be recognized, because it explicitly states that 'the improvement of the economic and social cohesion' is a fundamental goal of the socio-economic policy of the European Union and its member states. In the light of recent societal changes this goal seems to have become even more important. Dahrendorf et al. (1995) argue that the improvement of social cohesion is an essential condition for the creation of prosperity. They stress that a policy that aims to stimulate economic growth therefore must always pay attention to the social 'habitat'. In this period of economic globalisation, where social cohesion is being threatened by increased labour market flexibility and income inequality, this is of central importance. In this context, governments should try to maximize economic competitiveness, but at the same time try to avoid endangering social cohesion. This means that society needs to take steps to ensure that the transition costs of societal developments are not borne by the poorest and the most vulnerable in society (see also Miller, 1997;

Pearson and Scherer, 1998). Limiting inequality obviously impacts directly on the welfare of society but may have direct effects on efficiency by reducing crime and ill-health (Wilkinson, 1997; Kawachi and Kennedy, 1997) and by facilitating the acceptance of change.

Different interpretations of the situation facing European employment policies are reflected in the differences in policies. The UK with its traditional closeness to the USA has largely opted for the flexible labour market approach advocated by the OECD (1994). This implies decentralised labour markets with bargaining at company or plant level, low levels of legal employment protection, low benefit levels and tough eligibility criteria. Continental European countries such as Austria, Belgium, France and Germany have more centralised wage determination, high levels of legal employment protection, quite generous benefit levels and more liberal eligibility criteria. Scandinavia and Southern Europe are different again. Within each grouping there is considerable variability. The persistence of these differences and their coexistence with similar levels of employment performance indicates that the need for reform of employment policy and for tax harmonisation have been exaggerated (Krugman and Baldwin, 2000). Given the very limited extent of convergence of employment policy thus far it is difficult to see the emergence of a consensus on employment policy. General agreement is also lacking on the ideological basis of any reform. Thus the policy manifestation of the EES the guidelines for employment policies (Council, 2001) contain a mixture of approaches from reform of tax and benefit systems to reduce poverty traps and provide incentives, to the promotion of career breaks and parental leave.

These problems of differentiation, lack of consensus and absence of an agreed ideological basis of employment policy are compounded by the interventionism necessary to create a European Employment policy. The broad remit of employment policy means its reform is contentious particularly as at its heart is the social welfare system and the redistributive policies of the state. Negative integration is not a possibility here reform is required in some of the most sensitive of national government policies. Thus the OMC is not a means to facilitate the development of the Union final destination but a mechanism uniquely qualified to meet the requirements for co-ordination in this particularly difficult area of policy.

Concluding Comments

The EU finds itself at an uncomfortable juncture. On the one hand, there is a need to consolidate the economic policy framework sufficiently to make EMU effective and to ensure that the broader economic and social ambitions of the Union are achieved. This calls for fresh thinking about who does what in the policy framework and about the interplay between, and importance of coherence in, different policy areas. On the other hand, political imperatives combined with dismay about the conduct of some aspects of policy at the supranational level result in a reluctance to countenance the conferring of further competence on Brussels.

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¹ It is not of course eliminated because instability of the external value of the Euro remains.

² The Stockholm Summit further refined the overall target by setting intermediate targets for 2005 and adding a target for men and women aged 55-64.

³ Although the EES does not specifically target welfare systems its guidelines in practice require welfare reform e.g. the promotion of active rather than passive measures to tackle employment and the need for tax and benefit systems to be changed to avoid poverty traps.

⁴ Ageing populations which require pension reform are unlikely to support such reform because it will be increasingly difficult to gain the support of the median voter.

⁵ Paying benefits to the unemployed.

⁶ This of course followed the earlier paradigm shift of economics from Keynesism to monetarism.