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# How to spend it: Replacing the Globalisation Adjustment Fund with a Labour Market Modernisation Fund

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# How to spend it: Replacing the Globalisation Adjustment Fund with a Labour Market Modernisation Fund

Annual working paper on the economic dimension of EU integration

WP II / III Theories: Team 3 (D10b)

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**CONTENTS**



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## 0. Abstract

In this paper it is argued that the economics of the Globalisation Adjustment Fund are weak and its politics questionable, hence making its relevance doubtful and poorly providing for meaningful adaptation. A case is subsequently made for the establishment of a better financed Labour Market Modernisation Fund aiming at stimulating national labour market reforms, via rewarding effective policy effort and alleviating political economic constraints.

## 1. Introduction

The establishment of the Globalisation Adjustment Fund received wide publicity and, also, won praises from politicians and academics for clearly demonstrating that the European Union's commitment to free trade is coupled with compassion for those losing their jobs in the process. Nevertheless, at the time of its negotiation, namely following rejection of the Constitutional Treaty and the near collapse of negotiations for the 2007-13 EU financial perspectives, there were suspicions that the Globalisation Adjustment Fund was primarily destined to serve publicity purposes, whilst providing (certain) governments with some, admittedly little, leeway in their negotiating tactics in regard to the multiannual Community budget (2007-13). Apparently, those suspicions were largely fed by the agreement to keep the scheme's annual budget very low (at 500 million euros). Thus, some critics went a step further, arguing that the Globalisation Adjustment Fund was, in effect, going to be politically counterproductive, because it fuelled, perhaps unjustifiably, public attention to the social cost of globalisation, while being far from adequate in compensating for that cost. Finally, there were those who dismissed any expansion of Community involvement in employment and social affairs associated with increased Community spending.

Arguments about the Globalisation Adjustment Fund are certainly linked to the wider debate on EU economic governance and, in particular, the role of the Community budget. Therefore, they are very likely to intensify in the course of deliberations on the future shape of the Community budget, launched by the European Commission in September 2007 (Commission EC, 2007a). The main issues in this context are obviously two: firstly, whether there is sufficient justification for a Globalisation Adjustment Fund in its present or a reformed version and, if not, secondly, whether there is a better way – purpose and/or instrument – to spend Community financial resources currently available for the Globalisation Adjustment Fund, instead of simply putting them aside. As a matter of fact, in this paper it is argued that the economics of the Globalisation Adjustment Fund are weak and its politics questionable,

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hence making its implementation uncertain and poorly providing for a meaningful reform. However, contrary to demands for reduced Community social spending, a case is made for the establishment of a Labour Market Modernisation Fund, aiming at encouraging labour market reforms and details are given about how it should work in practice.

## 2. Why the Globalisation Adjustment Fund is not a very good idea

The suggestion for a special Community Fund, a Growth Adjustment Fund as was then named, aiming at assisting national (labour market) adjustment to economic shocks, was originally put forward, but not properly justified, in the European Commission's initial proposal on the EU financial perspectives 2007-13 (European Commission, 2004). Subsequently, President Barroso floated the idea for a Globalisation Adjustment Fund, which would assist member states in coping with the domestic distributional effects of globalisation, thereby supplementing national support for globalisation losers. President Barroso's idea was eagerly taken up by Prime Minister Blair when the United Kingdom assumed the Presidency of the Council of the EU – second half of 2005 – and had *inter alia* to steer negotiations on the multiannual Community budget towards successful conclusion. President Chirac, also, was unsurprisingly very supportive; after all, the Fund would likely signal that social Europe was still alive, thus warming up again the hearts of French citizens who had declared themselves opponents of a free-market Europe/ free-trade EU area.

In making the case for the Globalisation Adjustment Fund one of its leading proponents, Professor Loukas Tsoukalis, argued that the EU was in need of a stronger caring dimension, thereby responding to the adverse social consequences of international economic integration and industrial restructuring and reinforcing European solidarity, especially making it more visible in those parts of Europe that have not been benefiting from the structural and cohesion funds. A stronger caring dimension, in general, and the Globalisation Adjustment Fund, in particular, would, therefore, dispel perceptions of European integration as a mere vehicle of globalisation, and, moreover, increase confidence in European institutions which, also, have frequently served as a convenient scapegoat for unpopular policies at home (Tsoukalis, 2006). Besides being politically advisable, the Globalisation Adjustment Fund was economically justifiable too. Hence, it was argued that, following its being responsible for external trade policy, the EU should also undertake part of the responsibility – and part of the financial burden – for supporting workers displaced by international trade.

Furthermore, in view of the asymmetric effects of trade amongst member states, the Globalisation Adjustment Fund would only make the prospect of full trade liberalisation more likely, as it would ensure that, depending on the industry exposed to international competition, member states that would most benefit from trade liberalisation would, also, bear part of the cost which would heavily fall on other member states (Wasmer and von Weizsäcker, 2007).

Yet, for all its laudable purposes and the enthusiasm of its supporters, the Globalisation Adjustment Fund is not a good idea. In fact, it is economically unjustifiable and undesirable, socially immaterial and politically irrelevant and, perhaps, counterproductive. Thus, firstly, EU responsibility for external trade policy does not by itself imply that the authority – and the financial resources – for cushioning the adverse effects of extra-EU trade on within-country inequality be also transferred to the EU level, or, indeed, shared between the member states and the EU. Sharing of responsibility would only be advisable if national policies to support displaced workers were effectively undermined by pervasive cross-border externalities, but this may hardly be empirically sustained. [1] Besides, if justification for EU social policies was solely, albeit incorrectly, linked to the assignment of economic competencies, shared responsibility between the EU and the member states should also entail cushioning the social effects of restructuring associated with internal market competition and competition policy. To put it otherwise, EU responsibility for compensating the losers from economic restructuring should logically not discriminate amongst its causes, so long as the latter are shaped by policies which have similarly and exclusively been assigned to the EU, external trade (in goods) policy entailing executive EU powers and competition policy entailing regulatory and judicial ones.

Furthermore, being an EU insurance scheme, the Globalisation Adjustment Fund is likely to trigger perverse national behaviour, associated with moral hazard and consisting in policies that effectively impede structural adjustment, thus increasing the frequency and severity of trade-induced shocks and resulting in increased claims for EU transfers, thereby further discouraging structural adjustment. In addition, adverse selection, entailing separate pooling

[1] One may hardly suggest that what is true for general social policy, that is the absence of substantial detrimental cross-border effects on (national) social protection systems and labour market regulation, breaks down when it comes to particular aspects, like policies in support of certain groups of workers. Nevertheless, the same may not hold in the case of industry-specific, or effectively industry-specific social policies which tend to distort competition within the internal market (on the economics of social policy in the context of European integration see Begg et al., 1993, pp. 101-115; Bean et al., 1998 and Begg et al., 2007).

of good and bad risks - countries which are respectively better or worse at dealing with trade shocks – implies that certain member states, essentially those considered as better risks, may be reluctant to join a meaningful EU insurance scheme, in the form of a Globalisation Adjustment Fund. Moral hazard and adverse selection, then, may only allow for a poorly endowed and tightly regulated Globalisation Adjustment Fund, albeit one with little bearing on national social insurance and little effect on the welfare of trade-displaced workers.

At a more fundamental level, though, a policy exclusively addressed to the needs of losers from globalisation would only be advisable, on both efficiency and equity grounds, if the re-employment and wage prospects for potential beneficiaries were feebler than for similarly profiled workers displaced for other reasons, primarily technology.[2] However, there is no evidence to bear this out. On the contrary, empirical evidence suggests that in both the US and Europe (EU-15) the fate of workers displaced by trade is hardly distinguishable from that of workers displaced for other reasons (Wasmer and von Weizsäcker, 2007; but see the evidence in OECD, 2005, chapter 1). Yet, coping with displacement presents considerable individual heterogeneity in regard to age, education, vocational skills and tenure. Furthermore, whilst Trade Adjustment Assistance in the US, addressing dislocations of workers caused by trade, may be justifiable on purely political economy grounds (Baicker and Rehavi, 2004), given the lack of comprehensive unemployment insurance and widespread hesitation towards trade liberalization often escalating to (direct or indirect) protectionism, in Europe unemployment insurance is comprehensive and generous, sometimes causing disincentive effects, and trade protectionist sentiments are weak, at least much weaker than in the US (measures on individual attitudes towards trade are found in Mayda, 2007), hence questioning the political economy rationale of specific compensation arrangements for trade-displaced workers.[3]

[2] However, it certainly is noteworthy that globalisation is, within the present context and for the Fund's purposes, imprecisely equated with trade liberalisation and international outsourcing, therefore, leaving aside international labour migration and financial market integration.

[3] Thus, the argument in Wasmer and von Weizsäcker (2007) that support for displaced workers is more effective at removing trade protection than at allowing for speedier adoption of new technology – besides, modern Luddites hardly exist, as the authors rightfully note – has different (policy) implications for the US and EU. However, in the US the policy debate has recently assumed some European flavour. Thus, besides calls for making the eligibility criteria more accommodating and broadening the scope and increasing the generosity of Trade Adjustment Assistance, proposals for radical reforms have also been floated, ranging from eliminating the full payroll tax for all workers earnings below the national median (Scheve and Slaughter, 2007), to establishing a displacement insurance programme – essentially wage insurance in the form of wage supplements covering reemployment wage losses – for workers displaced for trade or other reasons, therefore substituting Trade Adjustment Assistance and, preferably, also entailing diversion of financial resources from the existing unemployment insurance system, thereby altering the scope of the safety net (LaLonde, 2007).

Being so, it is not surprising that the annual budget of the Globalisation Adjustment Fund is capped at € 500 million. Nor is it amazing that its scope, intervention criteria and range of eligible actions are limited and, along with the working procedures and managing rules, strictly regulated (Regulation (EC) 1927/2006 of European Parliament and the Council). Thus, financial contributions may mostly be provided in cases of mass layoffs (at least 1000 redundancies over a period of 4 or 9 months, depending on firm size, place in the production chain, industry and territorial effects) caused by substantial increases in imports into the EU, declines in EU market shares or delocalisation to third countries and may be made for active labour market measures that form part of a coordinated package of personalised services aiming at facilitating re-employment of redundant workers (Reg. articles 2 and 3). Importantly, the Regulation establishing the Globalisation Adjustment Fund explicitly excludes financing of passive social protection measures, [4] only allowing for the financing of special time-limited mobility allowances and subsistence allowances conditioned on job-search and training activities (Reg. article 3). [5] Financing of restructuring of companies or sectors is also excluded (Reg. article 6). Finally, it is stipulated that assistance from the Globalisation Adjustment Fund will only complement national actions and may not exceed 50% of the total costs of measures described in member states' applications for contributions from the Fund (Reg. articles 5 and 10). And it is also stated that at least one quarter of the € 500 must remain available on 1 September each year, in order to cover needs likely to arise until the end of the year (Reg. article 12). Thus, allocation of financial support is largely based on rules, leaving little discretionary power to the budgetary authorities.

[4] Nevertheless, some authors have argued that member states may be tempted to flout the rules and label unemployment assistance as active labour market policy, so long as the two are closely, indeed conditionally linked in most national systems. And consequently, they have called for a more focused, tighter ruled and allegedly more effective approach, specifically entailing financing of just two active labour market measures, namely wage insurance, essentially a make-work-pay policy, and mobility allowance (Wasmer and von Weizsäcker, 2007). However, those measures are not abuse-proof, as the same authors admit. Moreover, their effectiveness is crucially dependent on their interaction with unemployment insurance and is, therefore, determined by their relative generosity. Hence, it is anything but certain. Furthermore, so far as workers' mobility is restrained by various effective impediments, also including non-economic considerations, a modest mobility allowance may likely prove ineffective.

[5] Unsurprisingly, in contrast to the Globalisation Adjustment Fund, the US Trade Adjustment Assistance, especially following its 2002 merger with the smaller NAFTA Trade Adjustment Assistance scheme on the basis of the latter's more expansive eligibility platform, finances unemployment benefits, wage allowances and social provisions, mainly health insurance, whilst also allowing for some weakening of the required complementarity between passive and active measures (Baicker and Rehavi, 2004).

It could certainly not be otherwise. Even when leaving other – still, the most important ones – considerations aside, more discretion would at least require a (very) reliable estimate of the number of potential beneficiaries, in turn allowing for a safe prediction of the amount of support available per beneficiary. However, providing a reliable estimate of the number of potential Fund beneficiaries verges on the impossible (for a thorough discussion see OECD, 2005, chapter 1).

Wasmer and von Weizsäcker (2007) have come up with a very rough estimate of trade-related mass layoffs, but their very rough estimate might be seriously misleading, as implied by other studies (a comparative summary of studies is found in Table 1). In any case, though, the numbers are small.

**Table 1**: Potential Globalisation Adjustment Fund beneficiaries (various studies' estimates)

| | Wasmer and Weizsäcker (2007) | **OECD (2005)** | Eurofound (2006) |
|---|---|---|---|
| Original data source | Sources not specified; reference to the European Restructuring Monitor Database | European Community Household Panel (ECHP) | European Labour Force Survey |
| Time frame | Average annual (period not specified) | Average annual 1994-2001 | 2005 |
| Coverage | EU-15 and extrapolation to EU-27 | EU-15 (does not include Sweden) | EU-24 (does not include Luxemburg) |
| Proxy for total layoffs | Permanent job losses **(1)** | Displacement rates as % total employment **(2)** | Job separations due to restructuring **(4)** |
| Number of total layoffs | 5.7 million | 4.27 million – 5.64 million **(3)** | 9.6 million **(5)** |
| Of which trade-related | 10% of the total: 570,000 | ? | ? |
| Of which mass layoffs | 10% of trade-related layoffs: 57,000 | ? | ? |

**(1)** Number of workers who do not find a new job within the same calendar year in which they lose their job.
**(2)** Secretariat estimates based on ECHP data. Displacement rates range from 4.5% of employment in medium-international-competition manufacturing to 3.2% of employment in services. For the whole economy/ total employment the displacement rate is 2.8% (data and explanations in OECD, 2005, chapter 1, Table 1.1).
**(3)** Our own calculations, the lower one corresponding to the 2.8% for total employment and the higher one to 3.7% for employment in manufacturing.
**(4)** Number of non-employed persons who separated from previous job up to one year before. The following reasons for separation are thought of as providing a very broad measure of the impact of restructuring: dismissal (3 million), end of temporary job (3,67 million), early retirement (453,400), own illness or disability (690,300), other reasons (1,79 million), (data and explanations in European Foundation for the Improvement of Living and Working Conditions, 2006, pp. 45-55, Table 10).
**(5)** This number may considerably overestimate job losses owing to restructuring. See (4) above.

A small-sized Globalisation Adjustment Fund, partially addressing the needs of relatively few displaced workers may reasonably not be expected to have any noticeable effect on citizens' perceptions of European integration and the EU's caring dimension. Its symbolism may, thus, also fade away. What is more, the Globalisation Adjustment Fund may, despite all purposes, even fuel negative perceptions of the EU, in so far as, on the one hand, it signals acknowledgment of mounting, perhaps EU-inflicted pains from globalisation on the part of European political leaders, whilst, on the other hand, fails to adequately respond to those pains – or, for, the sake of precision, it largely leaves responsibility for compensating globalisation losers where it did and should belong. To put it otherwise, a small-sized, little effective Fund may likely give rise to false initial expectations which, inevitably, are later transformed into disappointment and bitterness, thus adding to mistrust of European institutions and, even, lending credibility to governments' rhetoric of scapegoating the EU for domestic economic ills and policy failures, as well as overdue, yet painful reforms.

Furthermore, failing to allay European citizens' negative perceptions and, maybe, implicitly, if little, reinforcing their anxieties in regard to trade liberalisation and international competition, the Globalisation Adjustment Fund does nothing to shorten the distance between public perceptions and the empirical world.[6] Sadly, from a quality-of-public policy perspective, this distance is even getting longer. Indeed, recent empirical research provides ample evidence against much publicised notions of global economic integration causing widening of inequalities within rich countries, which are, nonetheless, underpinned by respectable academic analyses mostly based on traditional trade theory (Hecksher - Ohlin and Stolper - Samuelson), or the (modifying traditional theory) specific factor approach (for a short review of the trade-focused research on the domestic distributional effects of economic integration, Verdier, 2004). Without intending to – nor pretending to – to adequately and justly refer to, let alone discuss, a vast and growing literature, we may find evidence that overall income inequality in many member states has, since the mid nineties, not virtually changed, although considerable increases have been observed in some low inequality, especially Scandinavian countries (Begg *et al.*, 2007). Furthermore, wage inequality has, at least in certain member states, for example Spain, been found decreasing (Izquierdo and Lacuesta, 2007), although, on the other hand, increased inequality in the distribution of market incomes, in general, both in English speaking countries and Germany, has mostly been driven by unprecedented rises

6 A similar argument is made by LaLonde (2007, p. 5) in regard to the US Trade Adjustment Assistance, namely that "…the linking of displacement assistance to trade has helped foster the false impression that displacement largely results from liberalized trade…"

in top wage incomes (Dew-Becker and Gordon, 2005; Piketty and Saez, 2006; Bach *et al*., 2007). Obviously, those latter changes may hardly be causally related to international trade liberalisation.

As a matter of fact, recent economic research – based on better quality and coverage datasets and accounting for recent trends – has shed more light on the relative impact of globalisation on income distribution, whilst also providing evidence on the processes and channels through which that impact is exerted. Thus, it has been argued that trade globalisation, partly associated with outsourcing, has little contributed to rising income inequality within the rich economies, especially the United States, and may even have caused less inequality, largely owing to the advanced specialisation of the domestic production and related employment and consumption developments (IMF, 2007, chapter 4; Lawrence, 2007; for opposing views on recent trade and outsourcing-related inequality dynamics see Krugman, 2007; also see Geinshecker and Görg, 2007 with evidence for Germany). On the contrary, widening of inequalities in the rich economies may, partly, have been brought about by outward foreign direct investment, largely associated with offshoring, which has reduced the domestic demand for low-skilled labour (IMF, 2007, chapter 4; for a more nuanced view see Ekholm and Ulltveit-Moe, 2007). And it may, also, have been caused by financial deepening, owing to the unequal access of rich and poor segments of populations to finance.[7] Nevertheless, skill biased technology has equally, if not more importantly, influenced inequality, especially wage inequality, within the rich economies (Begg *et al*., 2007; IMF, 2007, chapter 4). Yet, disentangling the effects of technology and globalisation may empirically be daunting, also being conceptually questionable. However, the impact of both technology and globalisation – of market processes – on income distribution has historically been mediated by norms, institutions and policies, thereby leading to different outcomes between the US and Europe, mostly in the form of increased wage dispersion and higher unemployment respectively. Furthermore, the relevance of norms, institutions and policies in explaining wage inequality and income distribution within the rich economies has certainly been reinforced by the aforementioned recent empirical findings attributing inequalities to unprecedented rises in top wage incomes. The latter have, thus,

[7] On the other hand, though, financial deepening may provide for household income insurance and consumption smoothing and, even, substitute social insurance, which might be costlier to implement, yet more needed, at times of rising international economic integration (Bertola, 2007). Being so, financial education may be all but essential for improving and making access to credit and financial markets equal.

largely been accounted for by institutional and policy reforms that, primarily in the US, make winner-take-all outcomes more likely (Levy and Temin, 2007).

The normative case for (direct) trade protectionism being largely abandoned (see Bhagwati, 2007), economists and political scientists have focused on the domestic political economy of trade globalisation, mainly, though not exclusively (for example Rodrik, 2007),[8] dealing with the domestic policies and politics of socially responsible and (hence) politically viable trade integration (to borrow and amend the title from Verdier, 2004). Thus, there chiefly are two, yet closely interrelated channels through which governments may impact on the social and political dynamics of globalisation, namely the labour market channel and the preference formation channel. Alas, European governments have so far been little able or willing to exert their influence through either channel.

Firstly, most EU member states have put in place comprehensive unemployment insurance and assistance, thereby (for longer or shorter time) relieving the pain of displaced workers, including those displaced for trade-related reasons. Often, though, reemployment of displaced workers, including for trade-related reasons, has been a lengthy process, indeed lengthier than in the US, hence increasing the frequency of long term unemployment and inactivity, yet entailing small wage losses, indeed much smaller than in the US (OECD, 2005, chapter 1). This need not solely be a side-effect of generous European earnings-replacement benefits (see Sapir, 2005), but it may be caused by stringent labour market regulations, sometimes interacting with unemployment insurance, which slow down job turnover and labour relocation, thus making the gains from globalisation and technology lower than could otherwise be and, consequently, increasing the costs of adjustment. Apparently, reform of labour market policies and institutions has often been ill designed, or improperly implemented by European governments (see next section).

[8] Starting from the premise that trade and technology may have very different implications for procedural fairness, trade-related competition often being linked to deplorable and/or harmful practices (e.g. the so-called social dumping practices), Rodrik argues for the creation of a "policy space" for nations in order to handle the problems that openness produces (p.19-20). That policy space would *inter alia* take the form of a "broadened safeguard agreement", that is an agreement on social and developmental standards, that "…would enable countries to opt out from their international obligations under specified circumstances", essentially when "…the international economic transactions in question are in conflict with a widely shared social or developmental norm at home" (p.28). In making his case for "fair globalisation", though, Rodrik seems to be crossing the border of indirect protectionism. Besides, national comparative advantages may *inter alia* be sourced to widely shared social norms, hence their interplay may entrench, rather than threaten existing norms and broad institutional structures.

Secondly, although being largely shaped by cost- benefit expectations, of the sort implied by conventional models of the effects of trade on market income distribution, citizens' preferences for trade policy may, also, be influenced by other factors, such as social status, relative income, values, institutional affiliation etc. (Mayda and Rodrik, 2002; Merolla *et al*., 2001). At any rate, governments may well be able to positively impact on social preferences for trade liberalisation, primarily by persuading those who have little to lose and, perhaps, more, if indirectly, to gain to support trade openness and economic integration, an obvious example being workers in non-tradable sectors whose jobs are relatively secure and their purchasing power is increased. However, that impact might actually never be felt when governments, like European governments, oppose further integration to safeguard the rents enjoyed by powerful domestic interests, as in the case of the directive on the trade of services in the internal market (Saint-Paul, 2005). And it may, even, turn negative when governments embrace indirect protectionism, often dressed up in the language of social dimension, yet reducing the gains from integration, as with the abolition of the country-of-origin principle in the directive on the trade of services (De Bruljn *et al*., 2006). Finally, social preferences for trade and economic integration may weaken when, instead of addressing domestic economic ills and institutional failures, governments either engage in EU scapegoating rhetoric or/and adopt measures of largely symbolic value, thereby raising false expectations, as with the establishment of the Globalisation Adjustment Fund.

The Globalisation Adjustment Fund commenced operations in January 2007 and, thus far, only € 18.6 million of funds have been allocated in favour of 895 workers in the French car sector (€ 3.8 million) and 4,218 workers in the mobile phone sector, of which 3,303 workers in Germany (€ 12.8 million) and 915 workers in Finland (€ 2 million). Interestingly, in the case of the French car sector, assistance has been targeted at redundant employees in suppliers of car producers Peugeot-Citroën and Renault, while assistance to trade-displaced workers in the mobile phone sector has almost entirely been granted to redundant employees of a German (BenQ) and a Finnish (Perlos Oyi) manufacturer. With the exception of the Finnish case, where the Fund contribution has been justified on the basis of the serious impact of redundancies on the local labour market (Reg. article 2(c)), eligibility for Fund support in the other three cases has exclusively been related to the scale of redundancies (at least 1,000 over a 4-month period, Reg. art. 2(a)). [9] It certainly is noteworthy that in the case of the German company BenQ, which has taken up more than three fifths of the money thus far

[9] Yet, as just previously noted, even in the Finnish case there had been no less than 915 redundancies.

allocated by the Fund (€ 12.8 million out of € 18.6 million), nearly 80% of the Fund support (and of national co-financing) has concerned short-time allowances and mobility allowances (details of all cases are posted on the website of the Globalisation Adjustment Fund, http://ec.europa.eu/employment_social/egf/current_en.html).

The Globalisation Adjustment Fund has, thus far, spent conspicuously less than initially envisaged; what else could one infer when reading the regulatory provision that one quarter of the € 500 million remain available on 1 September each year to cover needs likely to arise until the end of the year (Reg. article 12)? At the time of writing there were six applications pending for Fund support, three from Italy, and the rest from Spain, Portugal and Malta, in total requesting € 61.6 million. Even assuming that all applications were approved, utilisation of the Fund would still remain minimal, hence making its impact virtually unnoticed. Finally, no application for Fund support has, thus far, been submitted by any central eastern member state, for reasons ranging, probably, from differential industrial structures implying less exposure to extra-European competition, to the size distribution of firms and the quality of corporate management, to the efficacy of public administration. That may likely accord to the aforementioned original intensions, whereby the Fund should especially aim at making European solidarity visible in richer member states, which most contribute to the Community budget and finance the bulk of EU regional transfers. However, being in line with original intensions is a proof of consistency, but not of political wisdom, let alone fairness. One may, thus, plausibly argue that the selectivity of the Globalisation Adjustment Fund, in regard to its potential beneficiaries, may further subject its political viability to its size being small, its impact being, thus, negligible and its value being, hence, symbolic and, inevitably, depreciating.

## 3. Why we need a Labour Market Modernisation Fund and how it would work

The European economy (EU-27) has, since the mid 2005, been staying on a brisk growth path (3% GDP growth in 2006), underpinned by strong employment growth (1.6% in 2006) and accelerating growth of labour productivity (1.5% growth of real labour productivity per person employed in 2006). Although being essentially cyclical, the economic recovery of the EU has likely been entailing a structural dimension, associated with past structural reforms. Nevertheless, there still is a sizeable productivity gap *vis-à-vis* the US, especially pronounced amongst the new member states and largely accounted for by a gap in total factor productivity, whilst both the average rate of employment in Europe and the average number of hours worked per person employed considerably lag those in the US (Commission EC, 2007b). Raising employment rates and productivity growth has been a fundamental objective of the renewed Lisbon strategy – the Partnership for Growth and Jobs – which encompasses macroeconomic policy and structural reforms in product, financial and labour markets, its specification being detailed and implementation designed via the Community Lisbon Programme and the National Reform Programmes.

The case for labour market reforms, in particular, has lost almost none of its importance or urgency. Neither, though, has it been freed of the controversies that have historically shaped the politics of labour market reform, mostly domestically, but also, if secondarily, at the European level. Evidence suggests that labour market institutions have, since the mid 1970s, been growing more rigid, though not in all member states uninterruptedly and, often, in subtler ways than captured by existing indicators (Blanchard, 2005; Nickell, 2003). Labour market institutional rigidity has, thus, been associated with poor labour market performance and, especially, persistently high unemployment and low employment, as well as lessening the positive impact of product market liberalisation on productivity (Aghion and Griffin, 2005, chapter 4), whilst also being blamed for deepening and, mainly, lengthening the adverse labour market effects of macroeconomic shocks (Blanchard and Wolfers, 2000). Hence, in times of intense competition and quick restructuring, linked to technical progress and (product and process) innovation, market liberalisation, trade globalisation and international capital flows, the cost of labour market rigidities has considerably risen, either in the form of competitiveness losses, owing to unwarranted labour cost increases, and/or in terms of sluggish labour turnover, resulting from regulations severely constraining the workings of the (labour) market allocation mechanisms, and leading to slower productivity growth and heavier turnover and restructuring costs. Furthermore, the unequal distribution of turnover costs, especially unemployment, amongst groups of workers and across geographical regions has also raised doubts as to the equity implications of inflexible labour market institutions.

Nevertheless, labour market reforms have, very often, been hesitantly advanced and poorly designed and/or inconsistently pursued. Notwithstanding the increased pace and frequency of changes in labour market institutions and policies, especially since the mid 1990s, those changes have seldom been deep and/or comprehensive, although the extent of policy failure, primarily reflected in high structural and actual unemployment, was likely calling for farreaching, yet politically costly reforms. Reforms of labour market institutions have instead been mainly marginal in scope and scale and, also, encompassed measures almost equally split between those reducing levels of protection and those providing for increased protection, whilst occasionally comprising contradictory policies undoing one another over a short period of time (stock of reforms is briefly taken in Begg *et al.*, 2007, pp. 94-96). Marginal reforms, in particular, have often taken the form of (lighter) regulations applying to new labour contracts only, thus leaving the entitlements of incumbent employees, especially those employed under permanent contracts, virtually untouched and, consequently, resulting in two-tier labour market institutions – and dual labour markets. Furthermore, reform initiatives have unevenly been scattered across policy areas. In fact, initiatives have mostly been taken in the areas of active labour market policies, taxation and unemployment benefits, whereas little action has been undertaken in the areas of early retirement, disability benefits and employment protection legislation (for example, Arpaia *et al.*, 2005). Arguably, (revealed) government preferences for labour market reform have largely been shaped by political considerations, mostly related to opposition (support) to (of) reforms on the part of politically decisive labour market participants (Saint-Paul, 2000). Furthermore, implementation of labour market reforms has not proven much easier amidst weak economic conditions associated with a higher risk of job losses amongst employed workers, hence questioning, to some extent, the predictions of positive political economy. In fact, comprehensive reforms aiming at increasing labour supply have seldom been carried out under unfavourable economic conditions (Begg *et al.*, 2007, 97; Boeri, 2000).

The contribution of (past) institutional reforms to lasting improvements in European labour market outcomes has empirically been strongly confirmed, whilst it has also been made clear that in the absence of (pro-competition) supply-side reforms, labour market performance may little and/or temporarily improve, unless other favourable structural changes take place (for example, IMF, 2003, chapter IV; Nickell, 2003; Nickell and van Ours, 2000; on current improvements in German labour market performance see Burda, 2007a and b, but for a skeptical view about the impact and relevance of reforms see Carlin and Soskice, 2007). Related to that, it has been suggested that much of the recent improvement in EU labour markets has been brought about by wage moderation, prompted by competitive pressures and realized via social pacts, but not associated with reforms in wage bargaining institutions and/or non-employment benefits (IMF, 2003, chapter IV). Sustainability of wage moderation should, therefore, provide a reason for continuing and, even, intensifying labour market reforms. As a matter of fact, reform of labour market institutions might hardly be thought of as a second order policy priority, let alone a finished business, however ebullient headline indicators and/or forecasts of labour market performance might appear. Quite often, the devil is in the detail: for example, Austria has one of the lowest unemployment rates in the EU, but low labour force participation of older workers and long average duration of university studies might substantially distort unemployment statistics (Sherwood, 2006); also, Finland has enjoyed a spectacular economic and labor market recovery, following the exceptionally sharp demand shock and deep structural changes of the early 1990s, but the incidence of long-term unemployment is much higher than conventionally recorded, being technically concealed thanks to the widespread coverage of active (labour market) policy measures (Maiväli, 2006); and in Germany unemployment has recently been falling vigorously, but there still is a high number of people working in the low-wage economy, while at least 2.1 million Germans hold two or more jobs, in order to earn enough to live on (Williamson, 2007).

As a matter of fact, strong rises in the shares of so-called flexible forms of employment in some EU member states, especially fixed-term employment and temporary agency work, associated with partial relaxation of employment protection laws, have increased the frequency of low-wage employment and, also, led to precarious (and volatile) employment and lack of training for those working under flexible job contracts, hence negatively affecting productivity (Commission EC, 2006, chapter 2). The need for complementary and, arguably, more comprehensive reform of labour market regulations has, thus, been made clear. [10] It also has formally been acknowledged by national governments. Indeed, the Council of the EU has called for a "sustained reform effort", *inter alia* conceding that only limited progress has been achieved with respect to reform of employment protection legislation and pointing to the need for reforms that improve work incentives in the welfare schemes and allow for increased labour utilisation by raising both employment and the average number of hours worked (Council of the EU, 2007a). Moreover, the European social partners have further elaborated, as well as broadened and sharpened their common agenda for labour market reform (ETUC, BusinessEurope, UEAPME and CEEP, 2007). Importantly, within the context

[10] Yet, it is debatable whether the German's government decision to impose a minimum wage in the postal sector was an appropriate reform. Whether, in other words, a minimum wage would both lift the market income of low-wage earners and cause no adverse effect on their employment prospects. In fact, expectations soon turned negative when, in response to the decision, mailing companies, domestic and foreign, announced their intentions to slash jobs and/or cancel business plans, also accusing the government for (indirectly) protecting Deutsche Post, the former postal monopoly ("Minimum wage comes at a price", *Financial Times,* December 6 2007).

of the renewed Lisbon agenda for growth and jobs, labour market reform has strategically – and, also, cognitively and normatively – been enriched and consolidated, via advancing flexicurity as an integrated and, supposedly, (re)balanced approach towards modernisation of European labour markets and welfare models, yet allowing for differentiated pathways (Commission EC, 2007c; Council of the EU, 2007b).

However, for all their pronounced, renewed and refocused commitment to comprehensive labour market reform, national governments have certainly not trimmed their aversion to (electoral) risk and, thus, not lessened their intrinsic distaste for unpopular policies, although they often have poorly manipulated their own "survival algorithms" and, consequently, failed to (electorally) survive. [11] Being so, comprehensive labour market reform may hardly ever find its way into the legislative agenda, let alone be duly implemented, unless questions of political feasibility and issues of economic desirability are given appropriate weights and jointly addressed, that is unless labour market reform is dealt with along the lines of a solid political economic strategy. Some commentators have even suggested that, as a strategic exercise, reform is akin to war planning (Münchau, 2007). As a matter of fact, preparing for different political and economic scenarios, having a clear view of when to retreat and when to stand firm, knowing and letting people know when the (reform) process comes to an end, building and maintaining public support and, still, having a credible and sensible exit option may, all, contribute to minimising the loss of (scarce) political capital and, maybe, the risk of electoral defeat suffered by reform-minded, albeit successfully contested governments. Yet, improving the chances of comprehensive reforms being implemented may, also, largely depend on making benefits from reforms bigger and bringing them forward, whilst also discounting their costs and providing for adequate compensation to those bearing most of the burden. Reinforcement of labour market reforms by reforms in product and financial markets, along with appropriately designed welfare reforms, in other words coordination of structural policies, may probably allow for a better, fairer and politically sustainable distribution of benefits from economic and labour market reform (Blanchard, 2004). But that may fail to materialise if macroeconomic policies are not conducive to economic and labour market reforms, owing to their being poorly, if at all, coordinated with structural policies (Koutsiaras, 2001).

[11] The "survival algorithm" metaphor has originally been used by Michael Lipton to denote the strategy of minimising the risk of ending up below the subsistence level followed by poor farmers in developing countries (Lipton, 1968). Obviously, it went counter to the neoclassical postulate of poor but maximizing farmers, elaborated by Theodore Schultz, a Nobel Prize Laureate in Economics.

It precisely is for those reasons that, no matter the collective pronouncements of national governments, comprehensive reform of European labour markets may still be practically unattainable. Thus, firstly, coordination of structural policies and, for that matter, buttressing labour market reform with reforms of economic regulation and welfare institutions, is impaired by a fundamental, yet plausible asymmetry in the EU system of economic governance: while a great deal of product and financial market reforms are directly enforced and/or dictated by "Brussels", labour market regulation and reform is predominantly - and indeed logically - set and enforced by national political institutions, hence raising the risk of making labour market reform hostage to strategic behaviour on the part of governments and, perhaps, liable to collective action problems.[12] Arguably, soft – that is, not legally binding – coordination of national labour market policies and institutional reforms, as within the context of the European Employment Strategy, the Lisbon strategy (I) and, now, the relaunched Lisbon strategy, or, partnership for growth and jobs, may do little to remove that asymmetry, provide for effective coordination of structural policies, both at the national and the European level, and increase the feasibility of labour market reforms. In fact, there has been enough evidence to cast doubt on the relevance of those coordination processes in regard to motivating economic and labour market reforms (Begg 2006 and 2007). In the words of a recent Commission document, "[t]hese processes…have been successful in allowing the Member States and the Commission to define common goals; but less so in stimulating the necessary degree of ambition and policy efforts to reach these common goals" (Commission EC, 2007d, p. 10). One may also add that these processes have often enabled national governments to engage in scapegoating Community institutions, though unfairly and unproductively and, sometimes, even counterproductively. Yet, one may hardly dispute the benefits of structural policy coordination at both the national and the European level, associated with complementarities between labour market reforms and product market reforms and cross-border policy spillovers respectively. However, gains from joint action, as compared to scenarios where labour market reforms, or, structural reforms, in general, are implemented in one or some member states only, are empirically estimated to be modest,

[12] This has almost nothing to do with social dumping. It may instead refer to government choices to postpone or, simply, change the process and content of labour market reforms in anticipation of increased gains for growth and jobs owing to other member states' reforms, or, in relation to strategic wage bargaining and competitive wage setting by national trade unions and employers' organisations, or, even, in connection to demands for centralisation of labour market policy at the EU level – the so-called social Europe policy agenda – allegedly to ensure fair competition in the internal market (a level-playing field), but actually to externalise the cost of labour market adjustment to the detriment of other member states.

still being higher for the euro-area member states than for the whole EU-27 (Weyerstrass *et al,* 2006, chapter 6; Commission EC, 2007b, pp.73-76).

Furthermore, secondly, but more importantly, quite a few analysts have questioned the compatibility of the Lisbon agenda for economic and labour market reform with the overly cautious, stability-oriented macroeconomic policy framework established by the Maastricht Treaty and the Stability and Growth Pact. Thus, in regard to fiscal policy, which has unsurprisingly drawn most attention, it has been argued that tightly constrained (national) fiscal policies may actually discourage labour market reforms, as the latter frequently, but not always, cause temporary increases in the output gap which should certainly be averted via fiscal stabilisation measures (notwithstanding the favourable impact of reforms on potential output), often entail direct budgetary costs (Razin and Sadka, 2002), an obvious example being flexicurity policies (Zhou, 2007), and sometimes adversely affect the effectiveness of automatic stabilisers (Mabbet and Scheckle, 2007), hence calling for discretionary fiscal measures. Also, from a political economy point of view, labour market reforms may likely be conditioned on (budget-funded) compensation packages being granted to reform losers so that they stop resisting policy change, whilst relying on the use of scarce political capital which, though, is equally precious for fiscal consolidation purposes (Eichengreen and Wyplosz, 1998). Being so, the recent reform of the Stability and Growth Pact may, at least partly, address those worries, although much depends on its implementation. However, a loose implementation of the Pact would arguably jeopardise the credibility of its fiscal rules and, consequently, fail to deliver stability, solvency and long-term sustainability of public finances.

Yet, it is suggested that, even with tight and strictly enforced fiscal rules in place, monetary policy might still provide for a macroeconomic environment conducive to labour market reform, should it promptly take the expected (reform-induced) increases in potential output into account, thereby embracing an accommodating stance and, therefore, bringing employment gains forward and allowing for short-term budget improvements (a similar argument made in Buti *at al,* 2007). Nevertheless, this may hardly hold within the context of European monetary unification and may even totally lack relevance for the Euro-area member states. As a matter of fact, an accommodating monetary policy stance would probably entail a good deal of monetary easing in order to embolden incentives for labour market reform in each and every member state and, for that matter, make possible a better balance and more tolerable distribution of gains and losses (over time and amongst labour market participants). However, that may barely be the case within the Euro-area, where monetary policy is naturally set on the basis of Euro-area (weighted) averages, hence little taking into account (reform-induced) changes in equilibrium rates of unemployment and potential output at national level, and run by a conservative-central-banker type of monetary authority – the European Central Bank. However desired, a monetary stimulus to labour market reform may, therefore, be in short supply.

Thus, contrary to the often espoused there-is-no-alternative argument, European monetary unification may actually weaken the incentives for labour market reform, for the simple reason that, having lost control, either in its entirety or in part, of policy instruments to stabilise the economy, national authorities have less to gain from (labour market) reform, be it in terms of a looser monetary policy or, perhaps, increased fiscal discretion, compared to what would have been the case had they opted out from monetary union. On the other hand, of course, labour market reforms may be all but compellingly needed to improve national economic adjustment to asymmetric shocks (as pointed out in Sibert and Sutherland, 2000). Yet, this has so far failed to produce other than marginal reforms, which may have not much increased labour market flexibility and, probably, not provided for wide-ranging and/or lasting improvements in labour market performance. It, thus, appears that comprehensive labour market reform has probably been entrapped within a governance system that falls short of producing adequate incentives for that purpose, be they sticks or, most importantly, carrots. However, as it is argued in the following lines, a modest, yet innovative institutional change might do the job, or, at least, go some way towards doing it.

That modest, innovative institutional change would consist of establishing an EU Labour Market Modernisation Fund aiming at stimulating comprehensive, but politically costly labour market reforms, via financially supporting – in effect rewarding – implementation of those reforms on the part of national governments. In particular, financial support from the Labour Market Modernisation Fund might, largely, entail backing (national) government policies and supplementing (national) budgetary resources in order to attain a politically acceptable distribution of gains and losses from labour market reform, which might often imply compensating those incurring most of the burden. Therefore, justification for the Labour Market Modernisation Fund lies essentially with failure of EU policy means and processes currently in place to bear on the domestic political economy of labour market reform, a sanctions-centred approach associated with Community legislation, though, being socially undesirable, in other words suboptimal, and politically infeasible. Justification for the Fund is, consequently, tied to expectations for sustained improvements in labour market performance and more effective coordination of reforms amongst member states, allowing for internalisation of cross-border policy spillovers and realisation of (admittedly modest) gains from joint action and, also, raising expectations for an accommodating monetary and macroeconomic policy stance.

The Labour Market Modernisation Fund would, following the preceding analysis, take both the place and the dowry of the Globalisation Adjustment Fund. But it would certainly not assume the latter's tasks. Yet, funding for the Labour Market Modernisation Fund might and, indeed, should well exceed the €500 million ceiling applied to the annual budget of the Globalisation Adjustment Fund, an initial source of additional financing – that is, within the 7-year budgetary framework currently in place – being the funds committed but unused, in application of the *'n+2'* rule. Economic reasoning and political economy considerations lend support to this view and normatively reinforce it. Thus, firstly, being solely assigned the task of financially supporting – in effect rewarding – implementation of comprehensive labour market reforms and, therefore, contributing to improved, in particular speedier labour market adjustment to economic change, the Labour Market Modernisation Fund would largely act in a preventive manner, little resembling the insurance-like, corrective function of the Globalisation Adjustment Fund. The Labour Market Modernisation Fund would, hence, be little liable to the problems of adverse selection and moral hazard and, consequently, relatively freed of those objective, efficiency-related constraints to its spending policies, which plausibly apply to the Globalisation Adjustment Fund. On the other hand, though, one might arguably point to the risk of deadweight losses, arising from the Labour Market Modernisation Fund financing reforms that would have been undertaken, even in the absence of Fund support. Yet, that risk might largely be mitigated, provided that Fund support would only complement national financing of reforms – the so-called requirement of additionality would thus be put into effect.  Secondly, from a political economy point of view, unlike the Globalisation Adjustment Fund, the Labour Market Modernisation Fund would not, at any rate intentionally, favour certain member states or groups of member states, its political viability thus being less premised on a small budget, compared to the Globalisation Adjustment Fund, other things being equal.

Describing in a more detailed fashion the sort of comprehensive reforms (that should be) eligible for Fund support, one might, perhaps obviously, talk about measures (closely) reflecting and/or (directly) following the guidelines for the employment policies of the member states, which, along with the broad economic policy guidelines, are mostly meant to guide national economic and labour market reforms, thereby largely implementing the relaunched Lisbon strategy for growth and jobs (for the Commission proposal on the employment guidelines for 2008-2020, Commission EC, 2007e). However, it is only reasonable, in fact desirable, that financial support form the Labour Market Modernisation Fund should not cover actions eligible for assistance from the European Social Fund. Thus, the Labour Market Modernisation Fund should not support policies essentially active in character, including policies to expand and improve investment in human capital (for a detailed description of policies eligible for ESF support, see Regulation (EC) No 1081/2006 on the European Social Fund). Instead, it should support reforms seeking to stiffen competition in the labour market and remove or, in some cases, offset distortions, including compressed wage distribution, which reduce effective labour supply and make the search and matching processes lengthier and costlier than would otherwise be, thereby allowing for improvements in the allocation of labour and realisation of macroeconomic gains.

Similarly, support from the Labour Market Modernisation Fund might, also, be granted to policies which cater for asymmetric information in the labour market and lack of access to financial and credit markets, thereby providing for better quality of jobs and increased labour productivity, as well as income security, yet at a cost lower than would have been obtained, had the reform at hand not been implemented. For example, substituting higher unemployment insurance for stricter employment protection legislation, thereby increasing flexicurity in the labour market, would probably both raise the rate of employment and lower the unemployment rate (especially amongst certain groups of workers). On the other hand, though, support from the Labour Market Modernisation Fund should, as a rule, not be granted to measures which are likely to increase labour market segmentation and put long-term labour market performance at risk.

At this point it might be useful to give some real examples of labour market policies, or announced reforms, all found in member states' Lisbon national reform programmes for 2005-2008, which might, in principle, be eligible for support from the Labour Market Modernisation Fund. Thus, eligibility might be granted to Austria's new approach to employment protection legislation, consisting of transforming its severance pay system into a system of portable individual savings accounts and, for that matter, requiring employers to contribute 1.53% of the payroll to those accounts. It might also be extended to the UK's Pathways to Work scheme which is aimed at reducing the number of people on incapacity benefits by helping them find work, *inter alia* entailing a £40 per week Return to Work Credit to make work pay. Fund support might also be granted to Denmark's (active social) policy for the long-term unemployed and socially exposed groups, entailing cancellation of personal debt on the condition of its being followed by employment, education or rehabilitation of beneficiaries. Eligibility for support might also be granted to Denmark's policy to increase effective labour supply via a reduction of taxes on earned income, evenly divided between an earned income tax credit, aiming at increasing incentives to get a job, and an increase in the middle-bracket income threshold, aiming at increasing the incentive to work more if already employed. And it might, similarly, be extended to the Czech Republic's policy to motivate low-income groups to participate in the labour market via reducing the two lowest marginal tax rates and replacing standard tax allowances by tax credits. Fund support might, finally, be granted to the UK's New Deal for Lone Parents programme, *inter alia* entailing a work search premium, which is a £20 payment per week to lone parents undertaking intensive work search activity, as well as in work credit, offering additional support to lone parents leaving income support or the income-based Jobseeker's Allowance to get a job. The list of examples could certainly grow longer, still doing little justice to member states' successful policy efforts.

No doubt, the way the Labour Market Modernisation Fund might practically work, in particular configuration of the (operational) principles, (exact) eligibility rules, processes and evaluation methods governing allocation of its resources, should comply with the criteria of transparency, consistency, fairness, effectiveness and efficiency. Arguably, the trickier issue would most likely concern the choice of indicator(s) which should be employed in order to measure the (expected) impact of labour market policies and institutional reforms and, accordingly, determine the amount of financial support granted by the Labour Market Modernisation Fund (see below). Nevertheless, utilisation of Fund support would only be decided by member states, on the sole condition of its being complementary to national financial contributions. As a matter of fact, whether in the form of co-financing targeted wage subsidies in order to increase employment of less employable workers, or in the form of co-financing compensatory measures for those left worse-off, following labour market reform, or in the form of direct budgetary contribution, allowing for lower spending cuts and/or tax increases than would otherwise be, the Labour Market Modernisation Fund might help in alleviating the domestic political economy of labour market reform, its exact role and contribution being case-specific and policy (reform)-shaped.

At a more practical level, member states' applications for financial support from the Labour Market Modernisation Fund might be submitted annually, following submission of the Lisbon national reform programmes whereby implementation of reforms and progress achieved over the last year, as well as measures planned for the coming year are – should be – fully reported. Fund support should solely be sought for measures which, at the time of applying (for Fund support), have already been legislated and/or recently put in action. Furthermore, applications should contain detailed and readily observable information – at least partly included in the national reform programme(s) – in regard to the measure being put forward for consideration, such as: the measure's place within a broader in coverage and longer in time labour market reform programme/package, including its sequencing and possible complementarities with other policies and planned reform initiatives; the scope and (effective) coverage of the policy measure, including its likely being targeted at certain, presumably vulnerable groups of the labour force, eligibility for Fund support being denied when the risk for labour market segmentation is thereby higher, or, improperly discounted; the budgetary cost resulting from implementation of the measure under consideration, which might be variously sourced, as noted above, along with specification of the course of action where support from the Labour Market Modernisation might supplement national financing; finally and most importantly, estimates of the microeconomic (labour market functioning, e.g. location of the Beveridge curve) and macroeconomic (productivity, employment) effects of the reform under consideration, as well as in conjunction with other measures of the broader labour market reform package, based on a common methodology for assessing the economic impact of structural reforms, which has been developed and constantly refined by the Economic Policy Committee and its recently established Lisbon Methodology Working Group (Arpaia *et al.,* 2007; Dreger *et al.,* 2007; Sapir, 2007; Commission EC, 2007f).

Most crucially, then, the amount of financial support from the Labour Market Modernisation Fund might be linked to the estimated (reform-induced) employment growth, preferably adjusted for divergent job contracts, thus expressed in full-time equivalent employment. And it might, subsequently, be determined by the latter's multiplying with, say, one third of the unemployment benefit in force in the member state concerned. (Apparently, the exact amounts would largely depend on the Fund's total resources.) Furthermore, following a decision of the budgetary authority, based on a Commission proposal, to authorise support from the Labour Market Modernisation Fund, payment of the Fund's contributions might be extended over a period of two years, depending upon the implications of sensitivity analysis for the (expected) impact of the policy measure granted Fund support. However, reimbursement of the Fund's contribution might conceivably be stipulated, if the member state failed to comply with the obligations and commitments originally acknowledged in its application and then stated in the decision of the budgetary authority, or, when the policy granted Fund support, was repealed or effectively reversed, without proper – sound - justification.

Having said that, one might reasonably argue that the Labour Market Modernisation Fund should better merge with the European Social Fund, provided that its distinct function is carried out and resources are accordingly earmarked, yet allowing for a better coordination of EU spending policies and, maybe, a better targeting of financial resources on the implementation of the Lisbon strategy, whilst also affording realisation of scale economies. However, that might be inadvisable from the point of view of political communication, at least for a certain period of time. Thus, it should remain readily conveyable to the European public opinion that the Labour Market Modernisation Fund gives rise to a positive, pre-emptive EU role energetically anticipating economic change and helping member states to adjust appropriately, instead of merely responding to economic change but, often, with little appreciable impact.

Yet, beyond political communication and symbolism, the political advisability of the Labour Market Modernisation Fund might rest on two aspects. First, the Labour Market Modernisation Fund might be reinforcing national governments' effective power and strengthening their resolve for implementing much needed labour market reforms, thereby enhancing legitimacy in national political systems. Put otherwise, the Labour Market Modernisation Fund might be improving national ownership of the Lisbon strategy, unlike other procedural changes, thereby internalising (into the domestic political economy) attainment of Lisbon's objectives and fulfillment of commitments therein. Second, the Labour Market Modernisation Fund, unlike the Globalisation Adjustment Fund, would be making easier to shorten the distance between European citizens' perceptions of economic and social change and the empirical reality, instead of leaving it wide and, at times, increasing that distance, alas at the peril of democracy and prosperity.

## 4. A concluding remark

The debate on the future shape and role of the Community budget has just started – and it will be getting richer and stronger as time goes by. No doubt, reform of the Community budget is aimed at, *inter alia,* ensuring that EU expenditure is closely determined by and fully reflects the EU's variously ordered and structured competencies, whilst also serving its objectives effectively and efficiently. Establishment of the Labour Market Modernisation Fund might be a (admittedly small) step towards that direction, a step which would, nonetheless, adhere to both economic desirability and political feasibility, much unlike the Globalisation Adjustment Fund, which has inevitably been assigned an almost purely symbolic role, shaped by bad economics and equally bad, not the least divisive, politics.

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