# HOW SMALL COUNTRIES NEGOTIATE CHANGE

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- TWENTY-FIVE YEARS OF POLICY ADJUSTMENT IN AUSTRIA, THE NETHERLANDS AND BELGIUM -

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# 1. INTRODUCTION: BIRDS OF ONE FEATHER?

Austria, Belgium and the Netherlands seem 'birds of a feather', albeit with different colours (Alber, 1998). They are small and open economies, with a tradition of social partnership, a Bismarckian-type welfare state and a consociational democracy based on political coalitions that bridge cleavages of class, religion and language. A comparison of these 'most similar cases' (Przeworski and Teune, 1970) can potentially contribute to our understanding of the interaction between economic vulnerability, institutional capacity, policy legacies and policy responses.

'Birds of one feather, flock together', says the Duchess in *Alice's Adventures in Wonderland*. But in our case, they didn't. In response to the economic shocks of the 1970s Austria, Belgium and the Netherlands went different ways. Austria managed to keep unemployment low and was able to check inflation, whereas Belgium and the Netherlands accomplished neither. Why? Did policy-makers perceive or approach the problems differently? Did they act under different external and internal constraints? Did they pursue different objectives? When the oil shock of 1979 and rising interest rates in the 1980s had to be addressed, imbalances were much more pronounced in Belgium and the Netherlands than in Austria. But crises do trigger learning processes and create political conditions for change. This is most clearly seen in the Dutch case, where reforms in the 1990s were more daring than in Austria. Did the Dutch learn their lesson better or will they be just as vulnerable when another international shock hits? Why was in Belgium, despite very unsatisfactory labour market outcomes, learning of this kind blocked?

Our aim in this chapter is to present description and explanation. In this first section we offer a bird's eye view of the similarities and variations between our three countries. In the next three sections we offer for each country a dynamic, fine-grained account of problems, perceptions, legacies, policies and outcomes. The chapter ends with an attempt at explanation of the diversity in policy responses and policy responses, and an assessment of vulnerabilities and capacities.

## *1.1. Small and open economies*

Austria, the Netherlands and Belgium are three small countries bordering on Germany, their main trading partner (see Table 1). Belgium and the Netherlands trade heavily with each other, Austria with Switzerland and Italy. As transit economies, with the two largest ports of mainland Europe, Belgium and the Netherlands are two very open economies of Europe, with imports and exports making up 75% and more of their Gross Domestic Product. Austria's share is 60%, still above average in Europe but not unusual for a small economy. With limited domestic markets, these countries are highly dependent upon access to foreign markets and have always given much attention to trade liberalization and competitiveness. Unsurprisingly, they are advocates of European economic integration. Belgium and the Netherlands were among the six founding nations of the European Economic Community. Austria, a former member of the European Free Trade Association, joined the European Union in 1995. All three qualified for membership of the Economic and Monetary Union in 1999.

**Table 1. Austria, Belgium, and the Netherlands compared (1994)**

| | Population in thousands | GDP in million ECU | GDP / capita in ECU | Germany's share in exports | Openness of the economy * |
|---|---|---|---|---|---|
| Austria | 8.030 | 168.865 | 21.029 | 38.0% | 60.9 |
| Netherlands | 15.381 | 283.920 | 18.459 | 26.8% | 74.6 |
| Belgium | 10.116 | 193.610 | 19.139 | 19.4% | 81.4** |
| -- Flanders | 5.857 | 113.740 | 19.420 | - | |
| -- Wallonia | 3.538 | 50.538 | 15.274 | - | |
| -- Brussels | 950 | 29.332 | 30.864 | - | |

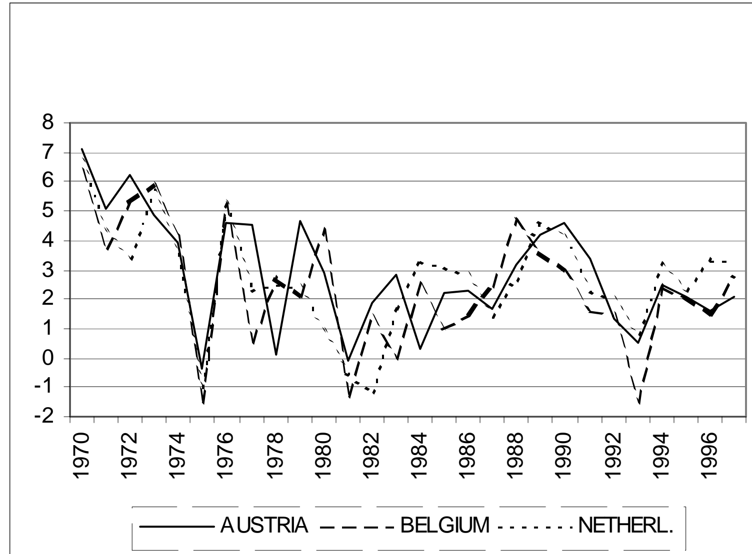
Sources: Eurostat, 1997; MPIfG, Adjustment Database, 1999: OECD, Economic Outlook 1999; and Belgian Statistical Office. * This measures exports and imports in percent of GDP. See: Schludi et al., 'Adjustment Data Base', Cologne, MIPfG, Table 3.2.4; ** including Luxembourg.

### *1.2. Different industrial profiles*

Small domestic markets encourage open economies to seek competitive advantage through product specialization and economies of scale in export markets. For historical and geographical reasons, our three countries exhibit different patterns of specialization. As the oldest industrial nation of continental Europe, Belgium developed a strong position in the production of raw material, coal and steel, and related industrial products, until decline began in the 1960s. In the past forty years, the economic axis has shifted to light industry and services, with a strong impact of the port of Antwerp and inward investment of multinational, mainly US-firms. The Netherlands industrialized late and never became a true industrial nation, despite its post-1945 efforts. The Dutch economy is specialized in transport and logistics, international finance, business services, agro-industry and foreign trade, a tradition that goes back to the seventeenth century colonial ventures of the Dutch East-India Trading Company. The country is home to large indigenous and Anglo-Dutch multinational firms, like Philips, Unilever, Shell, Heineken and some of Europe's largest banks. Post-war Austria lagged behind and still in 1970 12.2% of her labour force was employed in agriculture, compared with 3% in Belgium and the Netherlands. Today, Austria has a larger industrial sector in terms of people employed or value added. Unlike Belgium and the Netherlands, Austria nationalized large parts of industry and the banking sector after 1945. In the 1970s nationalized industry comprised 70% of banking, credit and insurance, 33% of industrial manufacturing, 23% of food distribution and 40% of housing construction (Kurzer, 1993: 38). The private sector used to be dominated by small and medium-sized firms and none of the major multinational enterprises had its home base in Austria.

The Netherlands and Belgium have no particular happy or interesting experience with industrial policy. After 1945 they undertook large-scale industrialization programs for the purpose of recovery of war damages (Netherlands) or development of rural areas, especially in Dutch-speaking Flanders (Belgium). In the 1970s both countries became increasingly immersed in hopeless rescue operations for ailing industries. At this time Austria showed less signs of strain and nationalized industrial firms maintained high levels of employment. But here the problems appeared in the mid-1980s, when under domestic and international pressure the nationalized sector was restructured and privatized.

**Figure 1: Annual real growth 1970-1998.**




*1.3. Growth, employment and unemployment*

On a cumulative basis, economic growth hardly differs between the three countries. All three experienced the slow-down in output and productivity growth that has characterized all advanced economies since 1973 (Figure 1). Until 1985 Austria did better. From 1986 to 1996 the economy grew with 21% in Belgium, 25% in Austria and 26% (the OECD average) in the Netherlands. The number of people in employment increased with 4% in Belgium, 6% in Austria (just above the OECD average) and 18% in the Netherlands. Labour force growth was much lower in Austria and Belgium, yet only in the Netherlands employment growth outpaced labour force growth. Hence, it was the only of the three countries in which unemployment in 1996 was lower than it had been ten years before (Figure 2). But the Dutch unemployment rate had to come down from very high levels. This predicament was shared with Belgium but had been avoided in Austria, where unemployment never exceeded 4% of the labour force until very recent. 1998 was the first time in two decades in which the Dutch unemployment rate dived under 4%. In 1998 Belgium unemployment fell to 8.8% (OECD, 1999b).

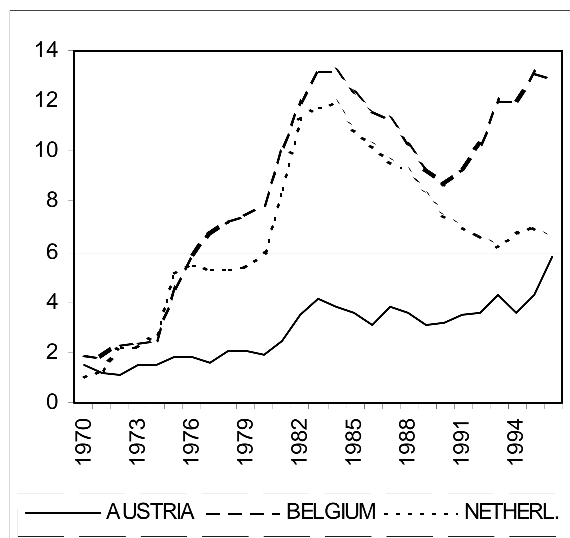
**Table 2: Output, employment, labour force and unemployment, 1970-1996**

| | Variability of output | employment responsiveness to output | labour force responsiveness to employment | variability of unemployment rates |
|---|---|---|---|---|
| Austria | 1.79 | 0.47 | 0.83 | 0.35 |
| Belgium | 1.88 | 0.45 | 0.15 | 1.40 |
| Netherlands | 1.55 | 0.52 | 0.12 | 1.02 |

Source: Pichelmans and Hofer 1999: 34. Belgium own calculations

The drama of unemployment was much larger in Belgium and the Netherlands and that Austria did remarkably well (Figure 2). How did this relate to the rather small difference in (accumulated) output growth? Figure 1 showed that the recession years of 1975 and 1993 were larger setbacks in Belgium than in the Netherlands and that the Dutch fared worse than the Austrians until the mid-1980s. Yet, Austria's output variability is not lower (Table 2). But through labour hoarding and labour force withdrawals (foreign workers, women) she matches output variability with considerable responsiveness of the labour force to employment opportunities, resulting in a much lower and hardly varying unemployment rate (Pichelmans and Hofer, 1999). This adjustment mechanism was not available in the Netherlands and Belgium. Foreign workers had obtained residential rights by 1975 and especially the Netherlands experienced strong growth of female labour supply, which was insensitive to cyclical demand changes (Hartog and Theeuwes, 1983). Overall, unemployment rates in Belgium and the Netherlands showed greater variation over the cycle (Table 2). Once unemployment is high and long-term unemployment is allowed to rise, it tends to be persistent (Layard et al., 1991; OECD, 1994).

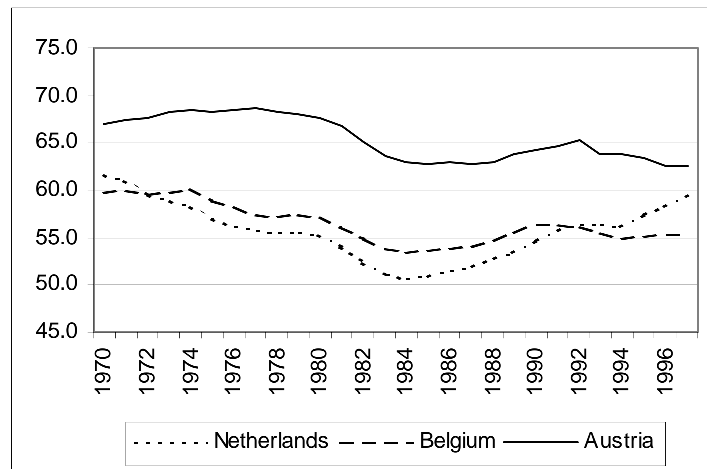
**Figure 2: Annual unemployment rates 1970-1997**




The catching up of the Netherlands is also shown in the employment/population ratios. Around 1970 the Netherlands, like Belgium, had one of the lowest employment ratios in Europe. This was at the time entirely due to the fact that married women did not take part in the labour force. After a further decline until the early 1980s, the Dutch employment ratio leaped from 50% in 1990 to 61% in 1998, almost level with Austria and five points above the OECD average. From Figure 3, based on data from the OECD Economic Outlook, we learn that over a thirty years period the Dutch are back were they were in 1970, with a rising line since 1984. Austria has been unable to continue its high level of employment of the 1970s and experience a decline in the 1990s. The Belgian development, starting from the same position as the Dutch and making an almost similar experience until the late 1980s, is characterized by downward drift and stagnation shows stagnation. The difference with the Netherlands is to be found in the 1990s.

Behind these trends there are significant shifts in female and male employment, a pattern of withdrawal of older males, a unique rise of part-time employment in the Netherlands, and very different employment levels and trends in domestic private services.

**Figure 3: Employment/population ratio's 1970-1997**




*1.4. Negotiated economies*

In *Small States in World Markets*, Katzenstein (1985) classifies our countries under the label of 'democratic corporatism'. In response to their dependency upon exports, the imperative of competitiveness and the inability to exert control over external events, small and open economies tend to develop tightly knit organized networks of consultative bodies at the national level oriented towards the advancement of economic and social progress, and the preservation of social peace. The *Parity Commission* (PK) and its various subcommittees in Austria, the *Central Economic Council* (CCE) and *National Labour Council* (CNT) in Belgium, and the *Foundation of Labour* (STAR) and *Social-Economic Council* (SER) in the Netherlands are postwar inventions. They embody the idea that Organized Capital and Organized Labour, together with state representatives and central bankers, share responsibility for the welfare of the nation.

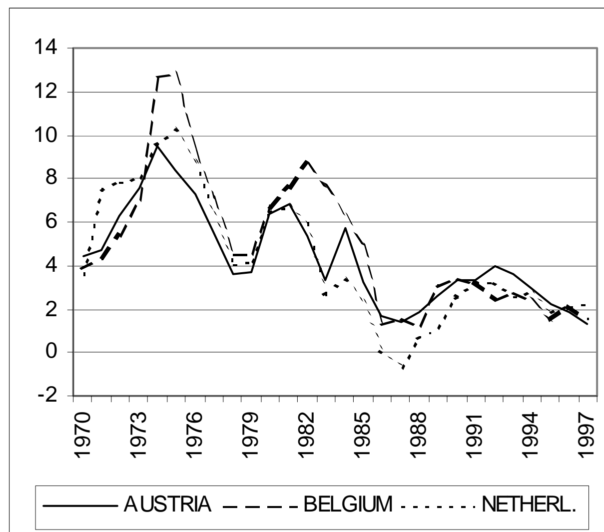
**Table 3: Some characteristics of labour relations in the mid 1990s**

| countries | Union density rate (total and private sector) | employees in firms joining employers' associations | Employees covered by collective agreements | extension of agreements through public law | national minimum wage |
|---|---|---|---|---|---|
| Belgium | 53 – 40% | 80% | 82% | significant | statutory |
| Austria | 44 – 37% | 96% | 97% | significant | agreement |
| Netherlands | 28 - 20% | 80% | 79% | limited | statutory |

Source: Visser 1996

In each country, the umbrella organizations of employers and unions are involved in consultation, between them and with the state. Overall, social partnership is more fully developed and stable in Austria (Tálos, 1997; Traxler, 1997) than in the Netherlands (Hemerijck, 1995; Visser and Hemerijck, 1997) and Belgium (Van Ruysseveldt and Visser, 1996; Vilrokx and Van Leemput, 1997). The state is weakest in Belgium, for reasons we will show later, while the co-operation between unions and employers is most balanced in Austria. Belgian trade unions count among the strongest outside Scandinavia (Ebbinghaus and Visser, 1999). They are more than in the other two countries integrated with and divided between political parties, and they must constantly perform a delicate balancing act between Belgium's two main linguistic communities and regions. From a comparative perspective, its central organizations of unions and employers are rather weak, with little authority over affiliates and pronounced regional divisions. Dutch trade unions weakened considerably between the mid-1970s and the mid-1980s, whereas Dutch capital and employers associations remain well-organized (Visser, 1997). In all three countries collective bargaining is pervasive and primarily organized by economic sector. In each country there is intensive co-ordination by the umbrella organizations, but in Belgium agreement has been rare. Dutch wage negotiators operate under a 'shadow of hierarchy'. The opposite trend is found in Belgian. Here the state has taken over the role of wage bargainers and negotiates under a threat of dissent and implementation failure. Table 3 captures some features of current labour relations.

***Figure 4: Inflation rates 1970-1997***

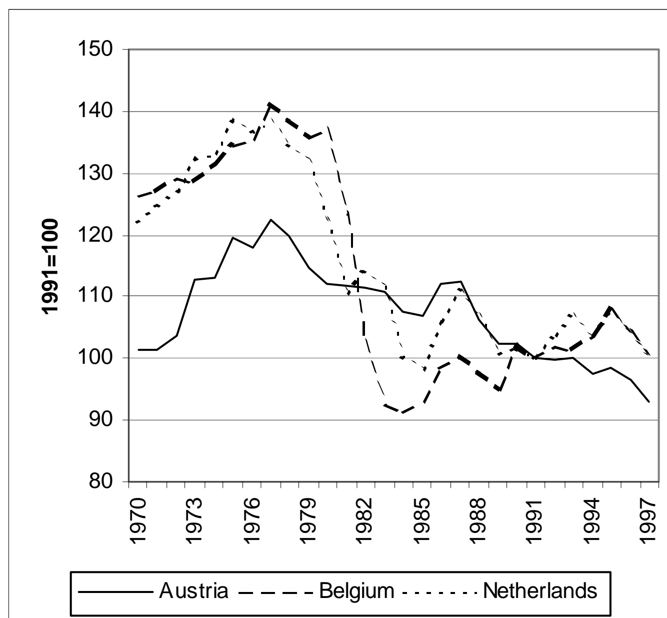



*1.5. Economic performance*

Institutional variation is associated with variation in performance. Austria had much less trouble with inflation in the 1970s than the other two. The Dutch had inflation quicker under control than the Belgians (Figure 4). Each of the three countries assigned monetary policy to the task, but Belgium and the Netherlands paid a high price in terms in terms of competitiveness. While the *Schilling* and the *gulden* were pegged to the *Deutschmark* in an early stage, Belgium had to

accept a major devaluation of the *franc* in 1982 and waited till 1990 before it tied its hands. Continuity in Austria and reversal of policies in Belgium and the Netherlands is well captured by the competitiveness indicator, based on unit labour costs in manufacturing (Figure 5).

**Figure 5: Index of relative labour costs 1970-97**




In the wake of the 1973 oil-price shock, policy makers in each country tried to combine a hard currency policy with Keynesian demand stimulation. But only in Austria congenial wage setting policies helped to avoid the negative outcome of cost-push inflation, a loss of competitiveness, and higher public debts. Austria (with Switzerland) was among the few continental European countries where levels of industrial and societal conflict had remained low in the late 1960s (Crouch and Pizzorno, 1978). Lijphart (1968) and Huyse (1970), when publishing their studies on the wonders of consociational democracy in the Netherlands and Belgium, noted that 'the times were changing'. Steiniger (1975), in his comparitive study, found no such changes in Austria.

Austria started the 1970s with a budget surplus and reached a maximum net deficit of just over -5% of GDP in 1995. The deficit varied with the business cycle but within the –5% margin. Belgium, where the net deficit peaked at -12% in 1981, shows the most extreme variation and managed with great difficulty to qualify for the EMU norm of -3% in 1998. The public sector deficit of the Netherlands peaked in 1982 at -6.6% and has declined since, approaching a balanced budget in 1999. The debt-output ratio increased in all three countries until the 1990s. Austria started with a low public debt of 19% in 1970, increasing to 69% in the 1990s until it declined to 64% in recent years thanks to austerity measures in 1995. Belgium entered the 1970s with a debt-output ratio of 64%, rising to a peak of 137% in 1993, declining to 122% in 1998 with the help of a special 3% EMU surcharge. The Netherlands began with 52%, allowed the debt-output ratio to rise to 81% in 1993 and than managed a reversal to 71%. The debt problem is reflected in debt interest payments, lower in Austria (3.5% of GDP in 1997) than in the Netherlands (4.3%) and Belgium (7.5%).

While Austria performs best in terms of the misery index (unemployment plus inflation rate), it

runs a slightly negative current account balance. Belgium experienced current account deficits and then also to a more extreme extent between 1977 and 1984. The Netherlands always had strong surpluses except in 1978 and 1980. The toleration of current account deficits in Austria may reflect the country's overall sound economic position and a monetary policy that is perceived as stable by international creditors.

The remarkable stability of Austria shows also in its functional income distribution. The share of labour in the national income has hardly changed during the past four decades. The slowly upward drift was reversed in the second half of the 1980s. In the other two countries, labour's share, adjusted for changes in employment structure, rose significantly after the mid-1960s and decreased in the early 1980s. In Belgium labour's share increased again in the later 1980s and in the 1990s. In the Netherlands a similar upward trend in the late 1980s was again sharply reversed after 1993. Labour's share in Belgian national income is above its 1960s average and above the European average, whereas it has fallen under its 1960s level in the Netherlands (Table 4). Underneath these trends, lie different wage policy experiences.

**Table 4: Labour's share in the national income, 1960-1997**

| country | 1960-1969 | 1970-1979 | 1980-1989 | 1990-1997 |
|---|---|---|---|---|
| Austria | 68.5 | 69.6 | 71.4 | 69.9 |
| Belgium | 69.6 | 74.5 | 73.2 | 71.5 |
| Netherlands | 69.9 | 74.2 | 67.6 | 65.8 |
| EU average | 71.3 | 75.2 | 73.1 | 69.9 |

Source: European Commission, DGII, *European Economic Review*, 4/1998 Adjusted for changes in employment structure

In terms of personal income distribution Austria is the most unequal of our societies. In 1993 the D5/D1 earnings ratio was 2.00 in Austria, against 1.43 in Belgium and 1.54 in the Netherlands (OECD 1996: 61-2). In the upper earnings range Austria is most and Belgium least unequal. Inter-sectoral earnings differentials in Austria are particularly large on account of inequality between male and female workers (Pichelman and Hofer, 1999). The incidence of low pay, or the percentage of workers who earn less than two-thirds of the median, is higher in Austria (13.2%) and the Netherlands (11.9%) than in Belgium (7.2%) (OECD, 1996: 72). Or should we say that wage compression at the lower end of the labour market is strongest in Belgium? The Belgian national minimum wage tends to be high by international standards. In 1993 medium wages in manufacturing were only 43% higher than the minimum wage, which is rather similar to the situation in German manufacturing. In the Netherlands, the distance between medium and minimum wage had risen to 56%, in France to 65% and in the UK even to 80% (Roorda and Vogels, 1997). In Austria minimum wages are contractual, vary by sector and are much lower in most services than in manufacturing (Dolado et al., 1996). If measured in purchasing power parity, the Belgian minimum wage is estimated to be about 10-20% above the Dutch minimum wage, which stood at just over Dfl. 2,000, or 1,120 Euro in 1999. More Belgian (9%) than Dutch (3%) workers actually earn the minimum wage (Roorda and Vogels, 1997).

### *1.6 Continental welfare states*

In the comparative literature on European welfare states, Austria, Belgium and the Netherlands

are classified under the regime-type of the continental, 'Bismarckian', conservative or Christian-Democratic welfare state (Esping-Andersen, 1990; van Kersbergen, 1995). Protection is based on employee insurance against occupational risks, financed by earmarked payroll contributions from employers and workers. Tradidionally, trade unions and employers' associations are involved in the supervision and administration of social security provision. Programs revolve around income replacement and are targeted at the male breadwinner in order to preserve traditional family patterns. In contrast to the Nordic welfare state model, social services are underdeveloped. Instead, the system is highly transfer-oriented. Active labour market policies are a recent discovery. In terms of resources spent on such policies in 1995, Belgian ranked at the fifth and the Netherlands at the sixth place out of fifteen European countries, after Sweden, Denmark, Finland and Ireland. If recalculated in percentage of GDP per percentage point of unemployment, Belgium (0.14%) trails the Netherlands (0.21%) but is ahead of Austria (0.09%) (OECD, 1997).

A comparison of policy provisions, concerning the social risks of unemployment, sickness, disability, poverty and old age, renders a differentiated picture of the three countries' social security profiles. Here we present the state of affairs in the early 1980s (Flora et al., 1986), in sections 2-4 we narrate the most significant changes and reforms. Unemployment insurance is compulsory in all three countries and financed by contributions from employers and employees, often with additional state subsidies. In the event of unemployment, dependent workers must register as unemployed and be available for work. Entitlement to benefits required a minimum record of 26 insurance weeks in the year preceding dismissal. Benefits were payable for 12 to 30 weeks in Austria; 26 weeks in the Netherlands, with an additional, lower but not means-tested provision for another two years; and without limitation but at a lower benefit level in Belgium. In all three countries insurance benefits are related to last-earned wages: from 58% for low-income to 40% for high-income workers in Austria; until a maximum of 80% (after 1987: 70%) in the Netherlands; at 60% in Belgium during the first year of unemployment, reduced to 40% in the second year for single persons, thereafter to a (non means-tested) flat rate of 50% of the national minimum wage. Family supplements, up to 80% of prior wages for the lowest income groups, are granted on application in Austria. In the Netherlands, people who are still unemployed after 2,5 year, were entitled to means-tested flat rate social assistance, guaranteeing 70% of the national minimum wage, with extra provisions in case of breadwinners. Trade unions in all three countries are involved in the administration and supervision of sectoral insurance funds, but only Belgian unions have a role in individual case handling of unemployed workers. This is generally seen as a powerful incentive for workers to join the union and an explanation for the high unionization rate in Belgium in times of high unemployment (Rothstein, 1992; Ebbinghaus and Visser, 1999).

All employees in these three welfare states are covered by sickness and disability insurance. In Austria, sickness benefits are payable from the fourth day of illness for a maximum of 78 weeks. Legally guaranteed benefits range from 50% to 75% of last-earned wages, depending on the length of illness, the degree of incapacity to work and family circumstances. Disability benefits vary from 60% of last-earned wages for single persons to 100% for breadwinners. In Belgium and the Netherlands sickness benefits are payable from the first day up to a maximum of one year, at a legally guaranteed level of compensation of 60% in Belgium and 80% (now 70%) in the Netherlands, though in most collective agreements this is topped up to 100%. After one year, Dutch workers qualify for a disability benefit, which is payable until the legal retirement age of 65 at a maximum of 80% (from 1987: 70%) of last-earned wages. The actual benefit level corresponds to the degree of claimant's incapacity. After one year of sickness leave, Belgian workers may claim an invalidity benefits of 65% of their last wages in the case of workers with dependent relatives and of 43,5% for single persons (subject to income ceilings). In Austria and Belgium disability coverage is restricted to accidents at the workplace and during the journey to and from work, whereas in the Dutch disability program entitlement is unrelated to the cause of

the incapacity.

Social assistance provides the public safety net for citizens who no longer have other entitlements or means of subsistence. Assistance programs are financed by general revenue, administered by municipal social service agencies, and subject to means testing. In the Netherlands, benefits are set at the so-called social minimum, since 1974 pegged at 70% percent of the national minimum wage for a single adult, 90% for a single-parent household, and 100% for a married or cohabitant couple. In 1974 a national 'right to a subsistence minimum' was promulgated in Belgium, with maximum social assistance amounting to 40% and 28% of average monthly earnings of an industrial worker in the case of married couples and single persons respectively. In Austria, social assistance falls within the jurisdiction of the provinces, which administer their own social assistance provisions, with significant regional variation.

The prior employment record is the main criterion for entitlement to old-age pensions in Austria and Belgium. Pension schemes are financed on a pay-as-you-go basis. In Austria, benefits can add up to about 80% of last-earned wages. There is no public basic pension in Austria and Belgium. In Austria older citizens in need must seek support from the family, voluntary organizations and social assistance. Since 1969 there is a minimum guaranteed income for the elderly in Belgium, providing a safety net for all senior citizens who are insufficiently covered by occupational pension schemes. Benefits levels of this scheme are flat rate, rather low and means-tested. The Dutch pension system has three tiers. The first tier is a basic public pension, which guarantees everybody over the age of 65 a (non means-tested) flat-rate basic income of Dfl. 1,400 (660 Euro). This part is financed out of general taxation and financed on a pay-as-you-go basis. The second tier provides for obligatory additional pensions, up to 70% of last earned wages. In contrast to Austrian and Belgian pension, this second tier is funded. The third tier consists of personal equity plans and other voluntary private pensions, many of which are tax deductible.

In the 1970s and 1980s each of the three countries used different social policy provisions to subsidise exit from the labour market and discourage entry. While in Austria early retirement and the repatriation of foreign worker provided for the main exit routes, in Belgium extended unemployment benefit performed similar functions, while in the Netherlands the generous and lenient sickness and disability pension became the main 'escape route'.

The three countries reveal similar trends in terms of total government outlays, resources spent on social expenditure, the share of social transfers, the financial basis of the welfare state, and taxation. In all these areas Austria was a laggard but has meanwhile caught up. Data for Austria show that total government outlays have continued to increase, while Belgium shows a decrease since 1993 and the Netherlands since 1988. Total government outlays were 53.2% in Austria, 55.3% in Belgium and 54.5% in the Netherlands in 1995. Social transfers in per cent of GDP were 22% in Austria, 24.3% in Belgium and 25.1% in the Netherlands. This share is increasing since the 1980s in Austria, whereas it is rather stable in Belgium and the Netherlands. Almost three-fifth is paid from social security contributions of employers and workers. In 1995 social security contributions covered about 57% of expenditure in Austria, 58.6% in Belgium and 59.5% in the Netherlands. The share of non-wage in total labour costs falls in midrange. Considering the whole tax structure, taxes tend to fall heavily on labour. According to the OECD (1998: 60), the effective tax rate, calculated as the sum of all taxes paid in the first instance by economic function, divided by the relevant tax base as measured in the national accounts, was 40% in Belgium, 43% in Austria and 46% in the Netherlands.

### *1.7 Segmented pluralism: class, religion, and language*

Austria, Belgium and the Netherlands have long been considered 'segmented' or 'pillarized'

societies (Huyse, 1970; Lorwin, 1971; Lijphart, 1968). In Austria, the two opposite sides reflected the class-divide between workers and owners, the latter including the self-employed, small business and farmers. They had before the war behaved like two separate societies or *Lager*, each with their own parties, unions, newspapers, sport's associations, para-military organizations, and clashed in a civil war in 1934. After 1945, with memories of civil war and Nazi-barbarism still fresh, they did much to invest in mutual co-operation.

Reformation and Counterreformation had divided the Netherlands between Protestants and Catholics, who in the process of development of mass democracy and worker mobilization emerged as self-contained communities or vertical 'pillars', alongside the Socialists and Liberals, each with their own parties, associations, unions, mass media, and clubs. Following the school pact of 1917, the leaders of these pillars learned to compromise and co-operate, while safeguarding a large degree of autonomy and control in the own pillar (Daalder, 1966; Lijphart, 1968). This system witnessed its maximum strength in the 1950s, but began to disintegrate with astonishing speed after the mid-1960s. Religious attendance and voting declined; Catholic or Protestant associations and parties disappeared or merged; the ties between interest groups and parties loosened; and elite control over society and in associations was diminished.

The class-division in Belgium was cross-cut by the division, between Catholics on the one hand and anti-clerical Liberals and Socialists on the other, over the role of Church and State in education, and by the language conflict between Dutch- and French-speaking Belgians (Lorwin, 1966). The school issue was finally put to rest in 1958, but the language conflict intensified. Within hundred years of the foundation of Belgium as an independent state in 1830, hopes for French as its sole, unifying language had vanished. The majority of the population spoke various local variants of Dutch, or Flemish, and many were alienated from a state that had most of the time been ruled by foreigners and long refused the use of Dutch in its laws, courts and high schools. Since French-speaking Belgians never had to learn Dutch, there was no basis for generalized bilingualism. Eventually Belgium became divided in three linguistic territories: a Dutch one, a French one, and a bilingual one, taking account of the reality of Brussels, a former Dutch-speaking city, located in Flanders, but gradually expanded and Frenchified throughout the 19th and 20th century.

The linguistic conflict was always contaminated by differences of class and economic fortune between the regions. Since the decline of the manufacturing and trading towns of Flanders, the province and other Dutch-speaking parts had been the backwaters of the Low Countries, whereas the mines and steel mills of Wallonia became the champions of 19th century railway capitalism. In the 1960s the economic position of the two regions began to reverse. Mutual distrust in the Belgian state channelled the preference of each community towards a federal solution: whereas Flemish nationalists wanted more cultural autonomy, Wallonia's Socialists and union leaders hoped to gain more economic power against what they saw as flawed policies from Brussels' *haute finance* and American capital. The Brussels conundrum ruled out a simple solution (Deschouwer, 1998; Van Parijs, 1998). The Flemish side defended devolution to language communities; Wallonia demanded regional autonomy; the French-speaking majority in Brussels feared Flemish domination as Flanders claimed Brussels as its capital. The solution that was eventually found was a double federation, i.e. a devolution into two, later three (taking account of a small German-speaking minority within Wallonia) language communities and three regions, producing five sub-national parliaments and governments (the Flemish community has merged with the Flanders' region). The powers and responsibilities of these entities have been defined in extremely complex negotiations, beginning with the fixing of the language border in 1963 (previously depending on a census in which people were asked what language they spoke). In 1993 Belgium was formally declared a federal state and, henceforth, all parliamentary bodies of the communities and regions are directly elected. The federation remains responsible for defence, justice, security, social security, labour law, fiscal and monetary policy. Foreign and European affairs are to be shared depending on the policy

issue at stake.

### *1.8 Consociational democracies*

The political systems of Austria, Belgium and the Netherlands, together with Switzerland, have been considered as the clearest examples of consociational democracies (Lipset and Rokkan, 1967; Lehmbruch, 1967; Lijphart, 1968). In such democracies party elites are encouraged to co-operate under a spirit of non-competitive power sharing. In his seminal theoretical case-study of Dutch politics, Lijphart sums up the ideal-typical consociational democracy as an alternative to the majoritarian Westminster model by four institutional characteristics: proportional representation, coalition governments, mutual veto rights, and cleavage autonomy. How well party elites are able to accommodate divergent worldviews in broad coalition governments, depends as much on institutional features as upon the preferences, strategic goals, power resources and control over their constituency of the various political actors. How policy choices effect policy performance, cannot, therefore, be answered by merely focusing on institutional characteristics (Scharpf, 1997). Only when grand coalitions adhere to common objectives and elites have control over their supporters, does consociationalism yield the institutional advantage of rash or consequent policy implementation. If, however, coalition partners adopt divergent policy goals or are faced with non-compliance and internal competition, they tend to engage in counterproductive political interactions, ending in policy immobilism. This was the fate of the divided governments in Dutch politics in 1970s and of the many large but unstable coalitions that ruled Belgium in those years.

The Austrian variant of *Proporzdemokratie* is rather unique, insofar its cleavage structure between the two pre-war *Lager* has translated into two large parties, both with a potential majority (SPO and ÖVP). From 1945 and 1966 they formed grand coalitions; in 1966 ÖVP formed a single-party majority that lasted until 1970, when SPÖ won the first of several general elections, allowing it to govern on its own until 1983, when it lost the absolute majority. In 1986 SPÖ returned to the grand coalition with ÖVP, continuing in the 1990s. The size of their combined electoral support has however decreased and this, together with the strong showing of the Free Democrats (FPÖ), a nationalist, anti-establishment party on the right, tends to threaten the continuity of Austria’s consociationalist-corporatist polity (Table 5).

**Table 5: Electoral results Social Democrats and Christian Democrats, 1975-99**

| year | Austria | | Belgium | | | | Netherlands | |
|---|---|---|---|---|---|---|---|---|
| | | | Flanders | | Wallonia | | | |
| | SPÖ | ÖVP | SP | CVP | PS | PSC | PvdA | CDA |
| 1976-80* | 50.4 | 42.9 | 12.4 | 26.1 | 13.0 | 10.0 | 33.8 | 31.4 |
| 1981-85 | 51.9 | 41.9 | 13.5 | 20.5 | 13.2 | 7.4 | 29.1 | 32.0 |
| 1986-90 | 43.1 | 41.3 | 14.9 | 19.5 | 14.6 | 8.0 | 32.6 | 35.0 |
| 1991-95 | 42.8 | 32.1 | 12.3 | 17.0 | 12.7 | 7.7 | 24.0 | 22.2 |
| 1996-99 | 35.6 | 22.6 | 10.1 | 14.5 | 10.0 | 6.3 | 29.0 | 18.4 |

* results are averaged for each interval in case of more than one election

SPÖ *Sozialistische Partei Österreichs*, ÖVP *Österreichishche Volkspartei*;

SP *Socialistische Partij*; CVP *Christelijke Volkspartij*; PS *Parti Socialiste*; PSC *Parti Social Chrétien*

PvdA *Partij van de Arbeid*; CDA *Christen Democratisch Appèl*

In the Netherlands coalition governments are the rule. The three main parties are, left to right, PvdA, CDA (before 1977 divided between a Catholic and two Protestant parties), and VVD, the conservative Liberal Party, which draws its support from the middle classes, white collar workers, and the business elite. Between 1945 and 1958 the government was built round the alliance between PvdA and the Catholic Party. From 1958 to 1973, with a brief interruption, the three Christian parties allied with the Liberals. From 1973 to 1977, around the first oil shock, PvdA dominated a centre-left coalition with two small left-of-centre parties and two of the Christian parties. From 1977 to 1989, with an interruption of only nine months, the government was formed by a CDA-VVD coalition, with CDA dominance. In 1989 it changed partner and allied with Labour. Since 1994 the governed is run by a unique Labour-Liberal coalition, forcing the Christian-Democrats for the first time in opposition since 1917. Electoral support for the traditional backers of the welfare state and Dutch corporatism, PvdA and CDA, has meanwhile dropped under 50%, as more voters shift their preference to the Greens on the left and the Liberals on the right.

The Belgian political landscape is more complicated and has in recent times undergone major changes. Between 1968 and 1978, the three mainstays of Belgian politics, Christian-Democrats (CVP/PSC), Socialists (PSB/BSP) and Liberals (PVV/PLP), did split in regional parties and are rivalled by regional competitors. However, the religious-ideological segments of like-minded political parties and trade unions, especially between CVP and the dominant Christian federation (ACV) in Flanders and between the PS and the socialist federation (FGTB) in Wallonia, have survived. The last all-Catholic cabinet dates from the 1950s, followed by a Socialist-Liberal coalition which in 1958 put the school issue to rest. The next forty years, Christian-Democrats ruled, in alternating coalitions with Socialists (1972-74; 1977-81 and 1988-99) and Liberals (1974-77 and 1982-87). Some of these Cabinets were enlarged by regional parties or have been based on grand coalitions of all major parties for the purpose of constitutional reform. Support for the Socialist and Christian-democrats has decreased and fell under 50% in the most recent general elections of June 1999. Belgium's federal government, and four of its five regional or community governments, are now based on a coalition of Liberals, Socialists and Greens.

### *1.9 Negotiated change under domestic constraints*

In small countries like Austria, Belgium and the Netherlands a sense of vulnerability is usually engraved in the minds of policy makers. External shocks induce policy actors to play down divisions though it may take time to understand the nature and implications of such challenges. Policy making in the three countries under study is critically dependent upon the agreement of different coalition parties and support from social partners. None of the actors is autonomous and free to choose its most-favoured response to new conditions or external pressures. This is particularly true for the government, whose role under rules of corporatism and consociationalism is constrained from without and from within. By incorporating multiple parties in coalition governments and integrating the social partners into the administrative structures of public policy-making, the state can mobilise more resources and rally support for policy change. But consociationalism and corporatism can also inhibit change, precisely because of the need for extensive compromises and coalition formation. All negotiated systems are vulnerable to so-called 'joint-decision traps' (Scharpf, 1988). Where the state is weak and its powers are 'hollowed out', this may create prolonged policy stalemates.

In the sections that follow we observe varying configurations of the relationships between state and social partners; from a very stable, uncontested and consensual pattern in Austria, a narrower, variable but in major areas regained co-operative style in the Netherlands, to a

disturbed and conflicting mode in Belgium. We will argue that this matters in the formation and implementation of policies in the field of wages, employment and social security, since outcomes do depend on co-operation, at different levels, between a variety of actors with veto power.

## 2. AUSTRIA: THE REWARDS OF SLOWNESS

Austria entered the 1970s with full employment and a sound macroeconomic performance. Its postwar economic policy profile was strongly influenced by the fact that all interested national actors shared the goal to free Austria from the surveillance of foreign occupation forces and re-establish a sovereign nation. This feeling of 'sitting in the same boat' explains the highly consensual style and the involvement of social partners in many policy areas. The cornerstone of Austrian social partnership is the tripartite Parity Commission with its subdivisions for Wages and Prices. It was founded in 1957, one year after the Hungarian uprising, under the threat of an influx of immigrants. The subcommittee for prices controlled about 80% of all consumer goods. Though the effectiveness of price regulation was contested and imported goods were beyond its scope, the committee did have a dampening effect on price developments and gave Austrian trade unions a unique position to influence wages and prices, i.e. to negotiate over real rather than nominal wages.

Austria's postwar model of co-operation between organized labour, capital and the state was embedded in a climate of consensus, based on a shared preferences for growth, exports, full employment, stability, social peace, and a deep fear of inflation. From the start, Austria's economic policy model included not only demand- but also supply-side elements, such as interest rate subsidies, export subsidies and guarantees, subsidies to tourism, and, above all, tax exemptions. The creation of the *Beirat für Wirtschafts- und Sozialfragen* in 1963, with representatives of the social partners and ministries, as well as academic experts, reinforced the 'expert' quality of Austrian social partnership. This Advisory Board issued policy recommendations on an allegedly scientific basis and became an instrument for orchestrating a policy consensus on the basis of a common understanding of the problems at hand. Implicitly, it was understood that the shared interests were those of Austrian male breadwinners. Negative effects, like the benign neglect of consumer interests and a bias against women and foreigners, were most of the time ignored by the social partners and by government officials. Also, Austrian unions had no explicit goal of narrowing income inequalities. Full employment, they argued, is the most effective income policy (Guger, 1998), while redistributive policies are best left to the state.

Collective bargaining in Austria essentially takes place at the sectoral level, but is highly co-ordinated via preparatory talks at the central headquarters of the social partners. The sectoral affiliates of the Austrian Confederation of Trade Unions (ÖGB, *Österreichische Gerkschaftsbund*) and the Austrian Economic Chamber (WKÖ, *Wirtschaftskammer Österreichs*, before BWK) negotiate over the wage level for each industry, but under strict supervision about when and how. Compulsory membership in the Chamber and the unitary structure of ÖGB produce an extraordinarily degree of discipline and membership (100% in the case of employers, 43% in the case of workers, down from 60% in 1970) (Ebbinghaus and Visser, 1999; Traxler, 1997). From the very beginning the peak associations were keen to prevent inflationary pressure emanating from competition between their affiliates. ÖGB always wanted to be involved in all areas of social and economic policy-making and not just be a 'wage machine'.

This encompassing view of trade unions was enhanced by the fact that the unions had a strong basis in Austria's unusually large public sector. After the war large firms were mostly nationalized

since indigenous big capital was scarce and the Austrian government tried to save them from the Soviet army's confiscation of German property. Nationalized industries in Austria accounted for about 20% of the employment in manufacturing, one-third of them working in the two main nationalized steel firms**.** But also the three leading banks, the mining, chemical and the engineering industry were practically under state control. Consequently, many of Austria's key industries were strongly unionized and in the mire of domestic policies, and they offered a useful tool to shelter employment if need be. In 1970 almost 80% of all employees in the public sector, adding up nationalized industries, rail and postal services, and government employees, were unionized, This compared with 54% in the private sector (Guger, 1998).

Macroeconomic policy during the era of postwar reconstruction emphasized cheap money, a balanced budget and a strong currency in order to dampen imported inflation. The Austrian Central Bank (ÖNB, *Österreichische National Bank*) was in part owned by the social partners and the political parties, with a 50% share of the state. This set the stage for a consensual and negotiated monetary and exchange rate policy. ÖNB pegged the *Schilling* first to the US dollar, then to a currency basket of her main trading partners and finally, in 1971, it joined the European currency 'snake'. Low interest rates set by ÖNB encouraged private investment by making loans cheaper. Savings were heavily subsidized in order to dampen consumption and encourage private investment. At this time, stable exchange rates with interest rate differentials between Austria and Germany could still exist, because capital controls prevented too large and sudden capital movements. In case of inflationary pressures, ÖNB put up credit ceilings. And as long as there was full employment, the budget was balanced or even in surplus.

### *2.1. Collective mistakes 'jointly corrected' in the 1970s*

Confronted by the first OPEC oil-price shock, Austria appears to have had the luck of the innocent. It had everything in place for an economic policy model that matched the requirements of fighting stagflation. The oil shock hit unexpected, as it did in other countries. With an expected inflation rate of 10%, unions and employers had agreed a 14% wage rise for 1975. When, contrary to the expected growth rate of 3,5%, a –2% contraction occurred, the social partners jointly 'corrected' their mistake (Scharpf, 1991: 56). The unions and the government assigned priority to full employment over real wage increases, redistributive objectives or budgetary restrictions. This even applied to the conservative opposition. The SPÖ government pursued an expansionary budget policy, including public investment programs and indirect subsidies to industry, in order to stabilize demand, while, in order to curtail inflationary pressures from abroad, ÖNB tied the *Schilling* to the appreciating D-mark. This 'unusual mix' (Guger, 1998) of policies proved extremely successful in countering the dilemma of stagflation. It could only work if every actor played its part and social partners were able to control inflationary pressures and prevent the erosion of competitiveness through wage moderation. The organizational strengths of the social partners, the encompassing corporatist framework and the consensus between them enabled Austrian social partners to do just that. Keynesian ideas had reached the Austria economic policy making community only late (Rothschild, 1993: 137), but in the 1970s the interaction of budget, monetary and wage policies showed a good fit with the prescriptions of Keynesian demand management.

This combination of deficit spending, hard currency and incomes policy was later coined 'Austro-Keynesianism'. It essentially revolved around five demand and supply side instruments, aiming at full employment and growth: deficit spending in order to stimulate demand; an accommodating monetary policy of low interest rates in order to stimulate private investments; labour hoarding in the nationalized industries; a hard currency policy; and an incomes policy. Austro-Keynesianism differs from traditional demand management in that it is not confined to anti-cyclical policies, but rather represents a long-term device to stabilize business expectations

with the help of incomes and exchange rate policies, encouraging growth and investment (Tichy, 1985). Employment stimulating budget measures were supported by cheap loans promoting private investment and allowing labour hoarding in the public sector. Inflation was held down by means of a hard currency and wage restraint. The commitment to fixed exchange rates necessitated that current account deficits resulting from such a policy had to be dealt with separately through export subsidies and taxes on imports.

Inflation came down from its peak of 9.5% in 1974. The increases in real wages during the recession of 1975 were compensated by subsidies out of the budget and corrected in the bargaining rounds for the next year. Since business could rely on moderate wage claims in the future, it needed not to increase prices. The hard currency choice helped to keep the price of imported goods low. Consequently, Austrian inflation fell rapidly in line with Germany. The comfortable budgetary position allowed adequate room for macroeconomic policy manoeuvre. 1975 was an election year and SPÖ, aiming at maintaining its absolute majority, gave priority to full employment and was willing to experiment with Keynesian deficit spending, overruling the traditional commitment to a balanced budget. The government allowed the deficit to increase from 1.5% of GDP in 1974 to 4.5% a year later. Since the budget deficit was to a large part financed abroad, the domestic money supply increased and crowding out of private investment through higher interest rates was avoided.

It has been argued that Austria's exchange rate policy in the mid 1970s was hard, whereas its monetary and labour market policies were soft (Breuss, 1978: 6). The currency policy of the early1970s was quite flexible and there were still signs of a visible autonomous exchange rate policy. Having depreciated by an accumulated –13% between 1968 and 1973, the *Schilling* appreciated 2.9% against the dollar from 1974 to 1977, helping to keep the price of imported oil down (Tichy, 1985: 500). Within the Social Democratic party, the unions emphasized the importance of stable exchange rates as a bulwark against inflation and the loss of purchasing power. As an alternative to depreciation, massive export subsidies helped to ease the burden on industry and help explain why Austrian exports (-3,5%) declined less than in Germany (-6.1%) (Uher, 1993: 86f). Trade unions did not take advantage of labour hoarding in the nationalized industries by pressing real wage increases, demonstrating that full employment was their true priority. Between 1973 and 1983, redundancies in the state sector were half of those in the private sector—indicating that the public sector did in fact shelter employment. It was a political decision that turned out to be an advantage once the crisis had passed. Nationalized industries were eager to exploit new market opportunities whereas comparable German firms were reluctant to hire new workers after they had made the experience of costly layoffs. The number of workers employed in Austrian industry fell only slightly in 1975-76 and increased immediately afterwards. An additional source of support for employment came from the service sector. Tourism, retailing and public sector jobs in municipalities, police departments and post offices soaked up those industrial workers who had been laid off (Scharpf, 1991: 58).

The demand-side success of Austro-Keynesianism was supported by fairly effective supply side measures. Firstly, like other European countries at the time, Austria implemented in the mid-1970s an already agreed reduction of the working week to 40 hours. Secondly, the government and the social partners jointly decided to operate a more restrictive quota of foreign labourers. The influx of foreign workers had played an important role in postwar Austria, helping to overcome the labour shortage during the period of reconstruction. Immigrant labour served as a buffer during the 1970s, when policy makers agreed to restrict immigration and encouraged repatriation, although not to such a large extent as was the case in Switzerland. A limitation in work permits resulted in a reduction of 52,000 foreign workers (-20%) between 1973 and 1978, equalling a 2% reduction of the labour force (Scharpf, 1991: 58). The combination of all these measures showed in low open unemployment and an increasing employment/population ratio, in spite of a slight decline in employment (-56,000) in 1975.

Chancellor Kreisky received a political bonus for his economic management in the elections of

1975 and, again, in 1979. Hence, SPÖ maintained its absolute majority throughout the crisis-ridden 1970s. Inflation was contained thanks to trade union wage moderation and a strong currency. Full employment was preserved because SPÖ privileged job creation, labour hoarding in nationalized sectors and repatriation of foreign workers over the goal of budget consolidation. Unemployment remained below 2% in the second half of the 1970s. The price of the hard currency option was a deteriorating external balance, but this seems not to have been a major constraint. The problem was addressed with an increase in the VAT rate on luxury goods and cars, intended to restrict imports, and through special investment and export promoting measures in the context of the Association Treaty with the European Community (Lehner, 1991: 474). Contrary to later periods, the confidence in the ability of national crisis management was high (Kienzl, 1993: 71). By achieving outstanding macroeconomic performance, while maintaining full employment in the face of the 1970s dilemma of stagflation, the policy-mix of Austro-Keynesianism, was raised to the status of a model of effective crisis management.

### *2.2 The policy of 'diving through' in the early 1980s*

The oil shock of 1979 in combination with the financial constraints of high interest rates in 1981 and increased international capital mobility posed a new challenge to Austrian policy-makers. This time they managed less well. The anticipated policy response to 'dive through' this second crisis in a manner that was tried and familiar, underestimated the changes in the international environment. The financing of the US current account deficit had absorbed 10% of world savings and high interest rates spilled over to Europe. The effectiveness of capital controls had eroded and international financial markets had become less predictable. This became evident in 1979, when ÖNB set interest rates below the German level.

The negative trade balance, due to the increased costs for oil imports in combination with low interest rates, resulted in a massive withdrawal of capital. ÖNB lost about one third of its reserves. This effectively caused the Bank to give up its active nominal interest policy (Winckler, 1980). The *Schilling* depreciated 2.3% against the D-mark in 1979 (Tichy, 1985: 500) and inflation increased from 1978 3.7% to 6.8% in 1981. Since all Austrian actors were afraid of depreciation and its inflationary consequences, the *Schilling* was officially pegged to the D-mark in 1980. By tying its hands, ÖNB sacrificed monetary policy in order to concentrate on exchange rate stability (Hochreiter and Winckler, 1996). The dramatic loss of currency reserves had persuaded the bank to abandon one crucial pillar of Austro-Keynesianism.

The budget deficit came under increased pressure of rising interest rates. In principle, the government applied a formula, which prescribed that the annual net deficit should not exceed -2.5%. Fiscal policy did not allow heavy deficit spending. But as in 1974-75, the recession of 1981-82 was fought with the help with expansionary employment programs, letting the deficit slip to -4% in 1983. Employment in the exposed sector was kept relatively constant, due to continued labour hoarding of the nationalized industries. Elderly workers were allowed to take early retirement. If unemployed, they received special allowances. Sending foreign workers home by withdrawing work permits, however, proved more difficult now, since many immigrants had, after a permanent stay of ten years, applied for Austrian citizenship. Still, banking on its successes of the 1970s, Austria managed to keep unemployment down at 3.5% in 1982. Full employment policy was not maintained, however. Using national rather than OECD or ILO statistics (the latter being more restrictive since they measure readiness to accept a job), unemployment rates had more than doubled within four years (from 2% in 1979 to 4.5% in 1983). The employment/population ratio fell from 68% in 1979 to 63% in 1983, reflecting early retirement and discouragement. Active labour market policies were hardly available. The favourable development in the 1970s had induced Austrian policy makers to continue without major changes, applying the rule: 'if it ain't broke, don't fix it' (March and Olsen, 1989).

Restriction of labour supply was a major policy response to the labour market problems of the 1980s. Giving in to union demands for a new round of working time reduction, two extra holidays were granted in 1985 and a year later minimum vacation was increased to five weeks, six weeks for workers with 25 years of service (Hauth, 1989: 19). In later years, negotiations over working hours were moved from national to sectoral negotiations, as had since 1982 been the case with wage bargaining. By the end of the 1980s, the average working week was 38 or 38.5 hours. Conditions for receiving disability pensions were eased and special allowances were available for redundant workers too young for early retirement but deemed too old for finding a new job. These arrangements, targeting firms in difficulties, were supported with public money and became in due course very expensive. Between 1975 and 1985 the number of older workers fell dramatically: while in 1975 98% of men and 47% of women between 55-59 participated in the labour force, these percentages had dropped to 70% and 30% in 1985. Participation rate of males aged 60-64 had halved from 38% to 18%; female rates in this age group decreased from 13% to 8% (Walterskirchen, 1997). SPÖ paid its reduced success in managing the 1981-82 recession with disappointing results in the 1983 general elections. The Social Democrats lost their absolute majority and turned to the then still quite liberal FPÖ to form a new coalition. In 1985 'Austro-Keynesianism', already dead by some years, was officially buried by the new SPÖ Chancellor, Sinowatz, when he observed that it had been a policy of 'diving through', which could only bring temporarily relief and never work in the long run (Seidel, 1993: 146). It had helped to retard the consequences of internationalization and prevented a rise in unemployment rates.

### *2.3 'Pulling the brake' in the later 1980s*

The new SPÖ-FPÖ coalition gave budget consolidation priority over full employment. Labour hoarding in the nationalized sector was increasingly seen as a burden on the public budget. The crisis of the steel industry became a factor in Austrian politics in the 1980s (more than ten years after Belgium or Germany). Between 1981 and 1985 the two major steel firms, Voest-Alpine and VEW, had received 25 billions ATS (3.6 billions DM) in subsidies. In 1985 VOEST needed another 16 billions ATS while, for the first time, it announced plans of a mass lay-off from 34,500 to 25,000 people, to be achieved by 1990. At the same time, VOEST Intertrading announced enormous losses from speculating on international financial markets. Consequently, the issue of privatization lost its taboo in the Austrian negotiated economy and labour hoarding in the nationalized industries was gradually abandoned. Finally, Austrian corporatism was willing and ready to go international but slowly, as summed up in a famous quote of ÖGB president Verzetnitsch: 'The most important person in a bob-sled is the one who handles the brake'.

The 1980s were marked by changes in policies, politics and perceptions. Nationalized industries were increasingly perceived as rent seekers. When the right-wing populist Haider took over FPÖ, SPÖ ended the coalition. After the elections of 1986, Social and Christian Democrats formed a grand coalition. The new SPÖ Chancellor, Vranitzky, came from the banking sector and was committed to a modernizing course. Both parties set their sights on membership of the European Union. They agreed on an extended program of privatization in 1986-87. Grudgingly and internallz divided, ÖGB went along, its member unions squeezed between the never-ending claims of the protected sector and a private sector which was less willing to foot the bill. WKÖ wanted privatization and deregulation, but slowly. 'Let up on the brakes but don't step on the gas' was the slogan of its general secretary (Teufelsbauer, 1986). The privatization program for 1987 left 51% of the shares of the public sector, including banking, Austrian airlines and energy firms, in public hands (Feuchtmüller, 1987). Privatization proceeded in steps and the consequences were cushioned with social plans elaborated by the social partners. This helped to keep unemployment stable at 3-4%. Yet, the abandonment of labour hoarding and the restructuring of

the nationalized industries—the most unionized sector and most stable electorate of the Socialists—led to a decrease in ÖGB and SPÖ membership. Under threat of losing their jobs, the frustrated workers became the ideal clients of an increasingly right-wing FPÖ.

In 1987, later than in most other countries, capital controls were abandoned. Now, the international judgement of Austria's economic performance became even more important. A sound budget figures high in international country ratings, which governments cannot afford to ignore. One convenient way to create revenue is to sell off the 'table silver' of state-owned enterprises, once they were restructured and stocks could be sold at a good price. Once again, this gave Austria time to postpone substantial social policy reforms. By the end of the decade, when privatization and industrial restructuring were well under way, the government finally managed to succeed in its consolidation effort. Helped by the expansionary effect of German unification, the budget deficit fell from 4.4% of GDP in 1987 to 1.8% in 1992. The tax reform of 1988 played a minor role in consolidation and was rather a step to adjust Austria to international standards. The employment effects were very modest (one calculation put it at a 0.2 percent point lower unemployment rate). Taking its cue from examples in the US, Germany and Sweden, the reform was meant to increase efficiency and transparency of the Austrian tax system by reducing exemptions in exchange for lower rates and a broader tax base (Nowotny, 1988). It was a political signal to capital that tax subsidies could no longer be expected (Lehner, 1991: 475). The corporation tax rate was reduced from 55 % to 30%, later raised to 34% again (comparable to Belgium with 39% and the Netherlands with 35%). Against international trends, the progressive element in the income tax system was strengthened (Guger, 1998), SPÖ and the unions continued to favour lenient treatment of small investors and savings accounts, many held by their members. The tax reform of 1993 abolished the inheritance tax and the tax on artisan enterprises. Austria appears to have the lowest property tax in the OECD (Farny, 1996: 74). As was discussed in the introduction, overall levels of taxation are slightly above the OECD average, though slightly lower than in Belgium and the Netherlands. The overall tax burden rose in the period up to the early 1980s but has been constant since, hiding a shift in the composition of revenues towards social security charges, now just over one-third of all revenues. Again, at this point there are hardly differences with Belgium and the Netherlands. The Austrian tax reforms of 1988 and 1993 shifted the tax burden from capital to labour. The effective tax rate on labour in Austria (43% in 1995) lies now between Belgium (40%) and the Netherlands (46%) and is not greatly out of line with other European continental welfare states (OECD, 1998: 60).

While reducing employment in the nationalized industries, Austria increased public sector employment, against international trends, even in Scandinavia. Government employment increased steadily from 8.9% of total employment in 1970 to 11.6% in 1980, 13.3% in 1990 and 14.3% in 1994. Between 1987 and 1996, the public sector, including education and health services, contributed to ease the labour market situation by increasing employment by 140.000, which is two-thirds of the total employment increase (Walterskirchen, 1997: 7). Most of these public service jobs went to Austrians, whereas foreign workers found jobs mainly in construction, retail, restaurants and manufacturing. In 1995 the federal government imposed an employment stop, and all increases have now to come from the regions and municipalities, responsible for education and health. Social Security and related public services expanded employment. Through the separation of the post office or Austrian railways from the state budget, now separate corporations, the government was able to generate new revenue.

### *2.4 The 1990s: going Europe*

The end of the Cold War and the opening of borders led to a revival of an old Austrian fear – to be left in the isolated corner where its capital geographically lies: east of Prague. Until 1989 Austria's place in the West had been assured by the Iron Curtain. To join the EU became now a matter of

utmost urgency. Back in the 1960s Austria had already applied for membership but the USSR had vetoed this. Its robust economic position, based on a hard currency, low inflation, low unemployment and close trade links with Europe and Germany, made Austria a sure candidate for EU membership. The budget deficit was the only cause for worry. The entry into the EU in 1995 and the austerity measures required to meet EMU membership criteria, became two showpieces of the resurgence of Austrian corporatism in the 1990s.

In the early 1990s, Austria's relative growth performance had improved and public finances were in good shape again. Though small by international comparison, Austria's labour market problems had however increased. Austria was heavily affected by the crisis in Yugoslavia. In 1991, an inflow from the traditional immigrant countries Yugoslavia and Turkey added 7% to Austria's labour force. Unemployment increased steadily, to 4.4% according to OECD and ILO statistics, 7.8% according to national statistics. This is still modest by European standards of today, but high if judged in the light of Austria's postwar accomplishments. Increased public sector employment and the effects of the introduction of the second year of maternity allowance helped to keep unemployment, but came at the cost of higher budget deficits. Under influence of lower growth rates, the deficit rose to 5% in 1995, despite consolidation efforts. From the tax side and the sale of state enterprises no alleviation could be expected. Substantial expenditure cuts became unavoidable. In order to divert from this unpleasant policy problem, the use of Brussels as a scapegoat was more than welcome to domestic politicians.

In the late 1980s, SPÖ and ÖVP had presented their ideas on joining EU and, after some massaging, convinced their social partners. This had been more difficult for the SPÖ than for the ÖVP. Initially, the unions received Vranitzky's liberal pro-European ideas with a great deal of scepticism. ÖGB was split between two wings, one in favour, led by the powerful metalworkers union, with mainly members in export industries, and one against, led by the union of white-collar staff in industry and services, now ÖGB's largest affiliates. ÖVP had to appease the opposition of small artisans and farmers. Farmers were induced to vote in favour of EU membership by the promise from industrialists to support liberalization of trade regulations, enabling farmers to earn money outside their traditional tasks. Later they reneged under pressures from tourism and retailing, and ÖVP had to orchestrate a new compromise, less favourable to farmers (Tálos and Kittel, 1998). In the end, Austrian social partners 'went Europe' and joined the grand coalition in its support of EU membership. In 1992, unions and employers negotiated an agreement in which they codified the switch from a closed to an open economy. A subcommittee for international affairs was founded and the long obsolete subcommittee for prices was changed in a subcommittee for competition (Nowotny, 1998). The hope to meet future shocks of internationalization under an EU umbrella, with closer ties to its larger German neighbour in such situations, had outweighed fears of a loss of sovereignty and lower social standards. After they had convinced themselves, the social partners played a leading role in persuading the public and in the 1994 referendum 66% voted in favour of EU membership, leaving only Haider's FPÖ and the Green Party opposed. Austria became a member of the European Union in January 1995, together with Sweden and Finland.

With EU membership Austria had set its sights at joining the EMU as well. It fulfilled effortlessly all the membership criteria, except the 3% norm for budget deficits and the 60% norm for the public debt ratio. A consolidation package of rather unpopular fiscal authority measures would have to be implemented. The social partners had been involved in virtually every major economic policy decision since the late 1950s. However, November 1994, for the first time in forty years, the government, after initial negotiations, decided to go ahead with its austerity plan without asking the prior consent of the social partners. Vranitzky was the banker-technocrat type of politician who had no close ties with the union leadership and even within his own party he was not fully supported. The ÖVP was split between the different interests of big industry, farmers, small business and artisans. Perhaps, the idea was that some demonstration of political power or public leadership was called for. The trade unions denounced the procedure as intolerable and stepped up

resistance. Their substantive criticism was that the package, including cuts in maternity and early retirement allowances, family assistance, unemployment benefits and civil servants pay, as well as higher contributions for health insurance, schoolbooks and public school transport, was socially unbalanced. This led to fierce tension between unions and party. The SPÖ was dependent on union support in parliament and the austerity measures that were in the end presented, and adopted, went less far than originally planned.

The unions had demonstrated their veto position but they were no longer gatekeepers. They could not avoid accepting the government's agenda and be drawn into negotiations over stronger austerity measures. But its failed show of political resolve had taught the government the lesson that it could not go against the social partners when making painful decisions. Yet, the conditions for co-operation had changed. The government decided the issues and the social partners worked them out (Tálos, interview September 1998). The second austerity package, of September 1995, was negotiated with the social partners, but was far more severe than the first one. It included expenditure cuts of 34.5 billions ATS (2.5 billion Euro), including a reduction in family assistance, birth assistance allowances, a cap on health care expenditure and stricter regulations on unemployment benefits. Furthermore, the Structural Adjustment Acts of 1995 and 1996 raised the threshold for early retirement, subjected disability pensions to stricter criteria and phased out the special early retirement schemes. Paradoxically, the social partners had gone much further than the government would ever have dared (Tálos, interview September 1998). The measures were implemented without protest—a unique feat in Europe.

### *2.5. Social policy: A pensioners' state*

As discussed in the introduction, Austria's social security has developed along the patterns typical for continental welfare states. It relies heavily on gainful employment and joint family coverage. This is reflected in the fact that about 95% of benefits are devoted to health, pension and unemployment insurance, plus family benefits, and only 5% to social assistance. Austria's policy of keeping overt unemployment low through the use of early retirement is clearly visible in the structure of social expenditures. In 1995, 49% of social spending went to old-age pensions, which is significantly above the EU-12 average of 44%. On the other hand and for the same reason, expenditure on unemployment (6%) is below the EU average (9%).

The 1995 restrictions in unemployment insurance increased the reference period from 20 to 26 weeks; benefits end after 20 weeks, though under conditions they may be extended to one year. Net replacement rates have been lowered from 58% to 56% of net wages. When unemployment insurance benefits expires, a means tested allowance, up to a maximum of 92% of the prior unemployment insurance benefit, is available under more restrictive conditions. The prolonged benefits for older workers or workers in crisis regions, introduced in 1990, have again been abandoned. Several local authorities, responsible for social assistance, have made payment contingent upon the willingness to work, introducing sanctions in the case of abuse and reducing benefits to asylum seekers (Alber, 1998: 18; Tálos and Wörister, 1998: 273-279). In the health system small user charges for hospital care have been introduced in 1989, in 1996 also for ambulant care (Tálos and Wörister, 1998: 230).

The main Austrian problem, so far unsolved, is the pension system. The 1980s and 1990s have transformed the Austrian welfare into a 'state of pensioners' (Esping Andersen, 1996, 4). Since 1975 the average retirement age of the dependent labour force has declined by roughly three years. In 1996 it averaged 58 years for men and 56.5 years for women (Pichelmann and Hofer, 1998: 9). In 1993, 2.2 times more transfers were spent on the old than on the young. Only Italy beats Austria in this respect. The Pension Reform 1997 raised the assessment base of pension benefits from 15 to 18 best years in order to harmonize the scheme with pensions for civil servants (Tálos and Wörister, 1998: 262). This change will be gradually phased in until 2003 and make it harder for

people with a short period in employment, in particular women, to draw a full pension (Alber, 1998: 14). Early retirement was made financially less attractive by cutting the replacement rate and terminating the allowances for pre-early retirement of the elderly unemployed. This has resulted in an estimated 7% curtailment of premature pensions being drawn after only 30 years of work (Alber, 1998: 15). The Constitutional Court has ruled against the unequal pension age of men and women, and women's pensions will now be raised from 60 to 65 years, to be fully phased in by 2024. Under pressure of the European Court of Justice, foreigners must be granted access to emergency aid. This is one of the few exceptions to the restrictive trend in social policy during the 1990s. The others are the introduction of care money for the old and sick, demanded by the SPÖ, and the prolongation of maternity allowances (to 18 months) and two years of unemployment insurance for employees who become self-employed, demanded by ÖVP and business groups. We agree with Alber (1998: 19) that the Austrian welfare state is still intact and no major shift towards a new welfare mix strengthening private provisions did occur.

### *2.6, The Alpen model: Success or failure?*

Austria's overall macroeconomic performance is quite good. Unemployment rates are among the lowest in Europe (4.4 % in 1999), though higher than what it used to be. Inflation is low, the current account improved from the international recovery and exceptional receipts from tourism. Income inequality is significant and increasing, but not an issue. Social peace and stability are still as solid as the Alps.

Schettkat (1999) used ILO data and called Austria one of the four European tigers, with the Netherlands, Denmark and Ireland, on account of their increasing employment/population ratios. However, our OECD Economic Outlook data, shown in Figure 3, suggest that Austria was rather a paper tiger. Employment displays a downward trend since the 1970s. There are too few new jobs for absorbing the increase in labour supply due to more women (re-)entering the labour market and immigrants seeking work. Employment ratios of people over 55 years are extremely low. Roughly four-fifth of job creation comes from the public sector, the major pillar of the employment policy of the 1980s and the 1990s. Between 1980 and 1996 50,000 new jobs were created in the private and 208,000 in the public sector. It is more than likely that this public job machine will not continue to work, due to further consolidation efforts. Recently, a trend towards more part-time employment is observed. In 1998 15% of all new jobs were jobs of less then 10 hours weekly, mainly held by women. But part-time jobs for women are often of inferior quality, and involuntary (Muehlberger, 1998), while socially unacceptable to men.

What is left, then, of Austro-Keynesianism? We have argued that this peculiar but successful combination of policies was abandoned in the early 1980s. Fifteen years on, upon joining the EMU, Austria has delegated monetary and exchange rate policy to the European Central Bank. The nationalized industries have progressively been sold off and privatization has been practically completed. Industrial policy is busy applying EU standards. In order to fulfil the conditions of the Growth and Stability Pact of the Amsterdam Treaty, further budget cuts have been proposed. These have to come from the expenditure side, for an increase in receipts in the near future is unlikely. The tax reform for the year 2000 is forecasted to result in a reduction of 30 billion ATS in government receipts. Trade unions wanted lower tax rates as compensation for real income losses in the last 15 years, the rest is for tax deductions of families, demanded by ÖVP. The original reform goal, as announced in the National Action Plan for employment submitted to the European Union, was to improve Austria's competitive position by reducing taxes and duties on labour costs, in particular through a reduction of payroll taxes in low wage sectors. But this was not realized. The employment effects will, hence, be modest and budgetary concerns paramount.

From the traditional Austro-Keynesian toolkit only wage moderation is left. Throughout the turmoil of the late 1980s and early 1990s, the Austrian wage bargaining system remained a beacon

of stability. Bargaining practices remained firmly entrenched at the sectoral level with the metal workers assuming wage leadership (Traxler, 1997). But what if unemployment keeps creeping up? Will the disillusioned trade unions demand higher wages for insiders? Will passive labour market policies be abandoned? Access to the EU Social Cohesion Fund has increased the attractiveness of active policies. Supervised by a tripartite board, the Austrian public employment service is managed by the social partners. The revised National Action Plan (1999) plans a reduction of the unemployment rate from 4.4% in 1999 to 3.5% by 2003 and the creation of 100.000 additional jobs. The emphasis is placed on reducing youth unemployment (Unger, 1998). There are doubts whether these measures will be enough to make up for the expected job losses in textile and clothing (-23,000 jobs), food manufacturing (-5,000 jobs) and building materials (-15,000 jobs)? Employment in services picked up, but slowly. In 1998 30,000 additional jobs have been created, mainly in the business related service sector and in retail, many of them part-time. Working time flexibility appears to be rather limited; compared with Belgium and the Netherlands, less Austrians work in shifts, at night, or during weekends. After considerable pressure of the government and heavy resistance of trade unions against amending the working time law in 1997, regulation on these matters has been devolved to collective agreement at the sectoral level.

In short, the Alpen model is rather old-fashioned. Despite the rhetoric of modernization, it is an example of 'defensive corporatism'. It continues to rely on the compromise of the social partners, with unanimous decisions between comprehensively organized peak associations, based on compulsory membership on the employer side and a monopoly of representation on the part of workers. Economically, it has not escaped the 'welfare without work' logic of continental welfare states. Exit from work has been the main strategy to keep overt unemployment low. Public employment has been the most important instrument in overcoming a lack of jobs. Job creation in private services has been lacklustre. Politically, the two big coalition parties have succeeded to continue their exclusive politics, but the challenge of the right populism of Haider has become stronger and is now a major obstacle in the continuation of the grand coalition. Socially, changes were mainly coming from abroad. Equal rights and affirmative action for women has been pushed on the Austrian agenda by the European Union and became law in 1995, after an impressive referendum result. A European Court decision has required Austria to end exclusion of foreigners from social assistance. The Austrian paradox seems that, with a high level of female labour market participation, higher in any case than in Belgium and the Netherlands, this society is still very male oriented.

The Alpen model has its minus points, but is it a failure? Is it a dinosaur, incapable of adjustment to the needs of post-modern society (Crepaz, 1995)? We prefer to speak of a midlife crisis of a 42 years-old social partnership, based on fears of faltering potency, the perception that the best years may be over, and the sudden engagement with a younger bride in Brussels (Unger, 1997). If there are signs of modernization, they essentially come from without—Europe—rather than from within. But a midlife crisis passes, even if the best years are over. Union density has fallen by one-third in these twenty-five years, and compulsory membership of the Chambers is challenged, but ÖGB and WKÖ are still formidable powers. In 1997 60% of Austrians (in 1983 69%) agreed that social partnership did a favour to Austria (in 1983: 69%), whereas only a small minority of 12% expressed the opposite view (Tálos and Kittel, 1998: 9). Referenda among members of the Economic Chamber and the Chamber of Labour produced a large turnout and considerable majorities in favour of continuation of compulsory membership.

The adjustment towards a flexible deregulated labour market progress faster than the public debate likes to admit. Many plant level agreements have flexible working time schemes, hardship clauses are used and firms in difficulties are exempted from sectoral collective agreements. In the retailing and building industry, in tourism and business services, regulatory flexibility has increased (BMAGS: 1999). This is part of the Austrian social partnership culture, which accepts internal flexibility, in particular when demanded by the works councils, which are above interested in the survival of their firm. Typically, they defend internal flexibility and deviance from the rules, while

defending strong external constraints, fixed in collective agreements and the law. In the process, Austrian social partnership has witnessed devolution towards sectoral negotiations and agreements. This implies some loss of central co-ordination capacities. Associational self-regulation is primarily confined to the areas of wage bargaining and vocational training. In short, the social partners no longer decide which issue should be on the public policy agenda. Rather they must deal with issues presented by the government, which itself is increasingly borrowing from the EU agenda. As the story of the consolidation package has so clearly demonstrated, the social partners are, however, still perfectly able to defend their institutional veto powers.

Of the three countries, Austria was least, and latest, exposed to the challenges of international trade. In combination with the extreme slow pattern of adjustment, this may have helped Austria to avoid extreme fluctuations in output and employment. Being a laggard, with about ten years of retarded development, has its advantages. In Nadolny's novel *The Discovery of Slowness*, the captain prevents his ship from being lost in the driving ice exactly because his innate slowness prevents him from reacting at once. Austria's entered the 1990s with lower unemployment rates and fewer fiscal problems in comparison with most other welfare states. Incremental or defensive corporatism was able to absorb external shock and to avoid internal upheaval, successfully shifting problems ahead and only solving the ones that were most urgent. The transformation of the welfare state has only just started. But the still existing strong institutional capacity of Austrian corporatism, as demonstrated in the accession to the European union and the 1995 austerity measures, means that the implementation of difficult changes, once the actors have decided, can be fast.

## 3. The Netherlands: Reinventing Itself

A distinctive feature of Dutch postwar economic policy was its stringent wage policy. Between 1945 and 1963, longer than any other western democracy, the Netherlands ran a statutory wage policy (Windmuller, 1969). Collective agreements needed prior approval from a Board of State Mediators, which was bound by wage guidelines issued by the Minister of Social Affairs. These annual guidelines were subject to central negotiations and intense consultation with the central organizations of unions and employers, which kept affiliates under strict hierarchical control. Statutory wage policy disintegrated in the 1960s under the pressure of tight labour markets and considerable wage drift.

After a failed experiment with self-regulation and intermittent state intervention, the new Wage Act of 1970 handed the responsibility for wage setting back to unions and employers. The government retained the power to order a temporary wage stop or impose a ceiling on wages, if the economic situation did in its view justify such a step. The unions opposed the law and temporarily left the main advisory body, the Social Economic Council (SER), in protest. Experience had told the Dutch unions that government controls placed them in the impossible position to defend low wages, whereas profitable firms, when under pressure, always broke the rules and paid higher wages. Not having control over the works councils, or otherwise present in the firm, this meant that government controls tended to 'hollow out' the bargaining role of unions and lead to membership disaffection (Visser, 1995). Distrusting the works councils and the government, the trade unions defended central wage negotiations, away from the firm, but without government involvement. Dutch employers likewise ruled out decentralization, since they feared that company bargaining would help a radicalizing union movement to enter the firm. Small and medium-sized firms lobbied for the continuation of government controls. Large and multinational firms might easily have done without and increasingly resented government interference, but they did not break ranks.

By the late 1960s Dutch wage policy, the distinctive element of postwar economic growth and

industrialization, was in shatters. Unions and employers were increasingly divided, even within their own ranks, over how to conduct a responsible wage policy and over the role of the government. They still maintained and would continue to maintain until 1982 the idea that wages should be determined centrally, with annual guidelines fixed by their central organizations in the Foundation of Labour. This led only once to agreement, in 1972, but that agreement was overshadowed by a leadership crisis in the Dutch Federation of Trade Unions and a strike in the metal industry over extra compensation for low-paid workers.

Comparing the Netherlands with Austria on the eve of the first oil shock we find opposite institutional conditions. While both countries had a legacy of centrally co-ordinated wage bargaining, this had broken down in the Netherlands and no alternative had yet been agreed upon. Institutional failure was aggravated by the rise in social conflict and breakdown of elite control, which accompanied depillarization. This was all the more serious because postwar industrialization, helped by low wages and rich natural gas exploits, had relied upon labour- and energy-intensive export products. As a consequence of large wage hikes in the 1960s, in essence the formalization of what some large firms already paid as 'black wages', the Netherlands had by 1970 become a high wage economy (Visser and Hemerijck, 1997). It could not sustain industries like coal mining, textile and clothing, and shipyards, and we observe that the decline in these industries began earlier, before the currency appreciation of the 1970s, and was more intense than in Austria or Belgium (in fact, in all European countries but Britain). This would have been less of a problem, had the Netherlands managed to match the decline in industry by growth in private or public services. But it did not and the entire 1970s were marked by a decline in manufacturing employment and a stagnation of private services.

### *3.1. The Dutch disease*

When the Bretton Wood system collapsed, the Netherlands joined the 'snake'. On this there seems to have been agreement among policy actors, reflecting a tradition of defending a strong currency and the placement of financial before industrial interests. This choice meant that if Dutch unions would prove unable to hold wages back, competitiveness would decline in case of an appreciating currency. This is exactly what happened, especially when Denmark, Italy, France and the UK defected from the 'snake'. Breaking the wage-price spiral became the key issue of the 1970s. Since labour costs in manufacturing were rising faster than in competing countries, all relevant policy actors agreed on the desirability of some form of incomes policy to combat cost-push inflation, but there was no agreement. On the eve of the first oil crisis, a left-of-centre government led by Den Uyl (PvdA) had taken office. Impressed by the recession but expecting the crisis to be of short duration, he opted for a Keynesian strategy of fiscal stimulation. The stage was set for a corporatist policy package, along the lines of the Austrian example, exchanging fiscal reflation for voluntary wage restraint. But the radicalized Dutch unions wanted more reforms in economic policy than this government, with weak support of its Christian coalition parties in Parliament, could offer. In 1974 the government imposed a wage and income stop, but its effect was undone as soon as the ban on increases was lifted.

Thanks to its gas exports, the Netherlands experienced no balance of payments problems after the oil price hike (the country itself was selected by the OPEC for its embargo). Hence an expansionary course seemed feasible and appropriate. There were various large employment programs but the main rise in government spending was on account of expanding welfare programs. This was in part the consequence of more people becoming unemployed or reaching the limits of their insurance and in part a concession to the egalitarian and solidaristic preferences of the unions. In 1974 the minimum wage, and, indirectly, public sector salaries and social security benefits, were 'linked' to private sector wage increases. Youth minimum wages sharply increased and were indexed as well. Most collective agreements contained automatic price escalators. The result was that pay increases in the private sector automatically translated

in a rise of public sector outlays. It made the government a prisoner to the outcome of negotiations in the private sector and an interested party in wage negotiations, which, unavoidably, became tripartite (Hemerijck, 1995).

From 1960 to 1980 the claim of the public sector on national income doubled. Between 1961 and 1971 the share of government outlays increased from 30 to 46% of GDP, to be compared with the rise of the OECD average from 30 to 37% (OECD, 1974). The share rose further to 60% by the end of the decade. This expansion was nearly solely caused by strongly rising transfer payments to households and, in later years, rising interest payments (de Kam, 1996: 263). The fast growth of the public sector was only in part matched by higher taxes and social security charges. Price indexation through semi-annual automatic cost-of-living adjustment of wages and benefits remained the main sticking point. The employer offensive to revise the system in 1977 was badly prepared. After a brief but massive strike the unions claimed victory. Consequently, indexation became the litmus test for solidarity between the high and low paid, and between those with and without jobs. It was hard to convince union members that they should give up this instrument at a time of high inflation, when it was needed most. Unlike Austria, Dutch unions were in the dark as to pricing decisions concerning common consumer goods. The rational expectation game of achieving lower prices and wages by anticipating lower wages and prices could not be played. The penalty paid by the unions for their defence of indexation was government intervention and an ever smaller space for negotiated nominal wage increases (Visser, 1990).

Indexation limits the room for manoeuvre in case of external shocks. International comparative data show that the short-term and long-term responsiveness of wage rates to changes in unemployment was much smaller in the Netherlands (and Belgium) than in Austria. Thus a much larger rise in unemployment was needed to induce wage moderation. Indexation tends to increase real wage stickiness. Indexation ‘tends to make inflation less painful and socially disruptive, but faster and more difficult to brake’ (Braun, 1976: 235). Since firms in the sheltered sector and government services do not have to fear a loss in market share, they can compensate higher wages by price increases with impunity. Like rising non-wage labour costs, higher prices in the sheltered sector end up, via indexation, in wage increases throughout the economy, undermining the competitiveness of the exposed sector. Indexation is associated with a higher overall wage level, since the ‘power of less favoured groups to insure that their wages rise more closely in line with other wages will probably not be offset by the reduction in the power of the most favoured groups to secure above average wage increases (Braun, 1976: 234)’. Dutch unions tried to negotiate lower increases for higher-paid employees, but this backfired when senior white-collar staff founded their own unions in the 1970s.

Natural gas turned out to be a mixed blessing, culminating in the infamous 'Dutch disease'. Apart from the embargo, the OPEC’s oil price hike should have caused a smaller problem to a country that had its own energy resources. Export revenue and import savings from natural gas resulted in a current account surplus, which put upward pressure on the guilder. The Dutch Central Bank (DNB) pursued its hard-currency policy with ever most zest when it realized that the government was losing control over wage setting and public finance. The effective exchange rate of the guilder increased by 30% between 1973 and 1977. Profits, real investment, net exports (excluding natural gas) and private sector employment came under pressure. The inconsistencies in the Dutch policy mix grew to self-defeating proportions (OECD 1980). In hindsight, one might have thought that policy actors might have been aware, that the combination of an appreciating currency, fiscal reflation and wage (cost) rises was bound to worsen the stagflation dilemma. In 1976 some prominent Labour Party economists called for a return to statutory incomes policy and stronger public sector expansion. But the unions rejected the proposal without so much as a thought. Employers did not want any further state influence and stepped up their ciritique against what they called ‘anti-business’ policies. In an unprecedented open letter to the Prime Minister, CEO’s of the nine largest multinational

corporations demanded in 1976 a change of government policy. The massive outflow of capital, from 2.3 to 7.5 billion guilders between 1972 and 1982 (Kurzer, 1993), was at the time widely seen as a vote of no confidence.

In 1976, Finance minister Duisenberg put on the brakes. Public expenditure should not rise with more than 1% of net national income per year (van Zanden and Griffiths, 1989). By moderating public sector growth the government hoped to make room for private sector investment. Den Uyl resigned the next year over the issue of land-ownership, won the largest-ever victory for his party in the general elections, but failed to form a new governing coalition. Van Agt, the leader of the newly formed Christian Democratic Party (CDA), brokered a coalition with the conservative Liberals (VVD). Like its predecessor, this government tried to talk trade unions into restraint, but it had even less to offer. Unable to bring public finances under control, it felt obliged to intervene in wage setting in 1979, 1980 and 1981, against its own intentions. The wavering position of the government was epitomised by internal conflict between the two CDA ministers of Social Affairs and Finance (Toirkens, 1988, Hemerijck, 1995, Snels, 1997). Albeda, responsible for Social Affairs, stressed the importance of co-operation with the social partners in fighting rising unemployment. Cuts in government expenditures and wage restraint were necessary, but had to be made acceptable to the unions through compensating policies. He rightly perceived a change in opinion within the trade union movement after 1978. Worried by continued decline in manufacturing jobs and the collapse of shipbuilding, the main union in industry made a U-turn and defended wage moderation in combination with working-time reduction. The union won the support from the Federation of Dutch Trade Unions (FNV) and late in 1979 there was even a draft central agreement in the Foundation of Labour. But FNV-leader Kok withdrew his signature at the last minute when opposing affiliates threatened with revolt (Nobelen, 1983). After this failed accord, so carefully arranged by Albeda, his Finance colleague, Andriessen, wanted an extended wage freeze for two years. As even VVD considered this demand as outlandish, Andriessen decided to resign. The commitment to concertation had triumphed over the objective of fiscal restraint, but not for long. When the second oil crisis hit, the Social Affairs Minister had no choice but impose another wage freeze.

### *3.2. The crossroads at Wassenaar*

The restrictive macroeconomic policies of the U.S., U.K. and Germany in the wake of the second oil shock increased the problems for the Dutch. The interest rate hike increased the financial liabilities of firms, squeezed profits and caused a spate of bankruptcies and factory closures. Unemployment soared at a rate of 10,000 to 15,000 per month, to a record 800,000 in 1984 (14% according to national statistics, later revised to 12% in accordance with ILO and OECD standards). Against the background of strong labour force growth, forecasts were extremely gloomy. Within five years trade unions lost 17% of their members and of the remaining membership nearly one-quarter was out of work, on social benefits or in retirement. The public deficit peaked at 6.6% in 1982.

Slowly but surely the relevant policy actors in the Dutch political economy came to understand the economic and social implications of the perverse spillover effects between high real wages, indexation, low profits, unemployment and fiscal crisis. In 1980, the Scientific Council for Government Policy issued a devastating report on the state of Dutch manufacturing and industrial policy, with a biting rebuke of the ‘waiting for corporatism’ attitude (WRR, 1980). Alarmed by its conclusion, Van Agt installed an ad hoc commission, chaired by the president-director of Royal Dutch Shell and members selected on personal merits (among others from the main industrial trade union). Not wasting time, this commission recommended that profitability needed a boost through lower wage costs, that wage negotiations required more

flexibility and decentralization, that wage differentials ought to increase, and public sector wages should be disconnected from the private sector (van Dellen, 1984).

The general elections of 1981 had resulted in a patched-up coalition between the Christian and Social Democrats, but the new administration immediately fell back into deadlock and lasted only nine months. New elections in 1982 brought an austerity coalition of CDA and VVD to power, thanks to gains for the Liberals. This 'no-nonsense' coalition, led by Lubbers (CDA), committed itself to a three track strategy of economic recovery through improved business profitability, lower wage costs, industrial restructuring and less regulation; reorganization of public finances and fiscal consolidation; and cost-neutral work-sharing in order to alleviate the unemployment problem. Unveiling its plans on 22 November 1982, the new cabinet declared that 'it is there to govern', with or without the consent of the social partners. Two days later, the leaders of the main union and employers' confederation, Kok and Van Veen, announced that they had struck a deal. This deal had been prepared in the Foundation of Labour (STAR) since the summer, but now the social partners were in a hurry to prevent another intervention. The government had already announced that it would suspend indexation in 1983 and its minister of Social Affairs, De Koning, bluffed that he might have to use mandatory work-sharing if there were no voluntary measures.

With unemployment running at double digits, another 14% on disability pensions and 6% on sickness benefits, the trade union movement was in no position to wage conflict. Employers saw a chance to rid themselves from recurrent state intervention (van Bottenberg, 1995). The Wassenaar agreement was a recommendation only, but one that carried authority. The opposition against the agreement—from the food and services union, to Philips and the metal employers federation—was defeated and isolated. Negotiators in sectors and firms were advised to forsake price indexation for the purpose of an improvement in investment and employment, and use the money for a cost-neutral reduction of working hours. With this agreement Dutch unions acknowledged that for a higher level of investment, essential for job growth, a higher level of profitability was required (Visser and Hemerijck, 1997). Like the government, employers recognised that working-time reduction was a small price to be paid for this concession. The response to the Wassenaar agreement was swift. Although negotiations over shorter hours proved cumbersome, in less than a year two-thirds of all collective agreements were renewed, mostly for two years, during which the payment of price compensation was suspended and a 5% reduction of working hours took place. By 1985, cost-of-living clauses had virtually disappeared; average real wages fell by nine 9% in real terms (Visser, 1990). The adjusted share of income from dependent employment, which had risen from an average 69.9% in the 1960s to 74,2% in the 1970s, fell to 67,6% in the course of a few years.

Assured of restraint, the government had its hands free to regain control over public sector finance. Between 1983 and 1986 a 3% decrease of the public sector deficit was achieved through a small decrease in employment (-1%) and salaries (-3%). In 1983 salaries, minimum wages and related benefits were frozen and for 1984 the government cut public sector wages with 3%. This brought the public sector unions in arms, but after a strike of three weeks they found themselves isolated. Formally, the government had ended the mechanism that since 1962 had assured public employees salary rises in line with private sector wages. Henceforth, unions and employers could no longer shift the costs of stagflation onto the government, but were forced to internalise the external effects of wage inflation and unemployment (CPB, 1997: 165). Private sector unions could no longer be held hostage by public sector unions (and benefit recipients). In later years this called for another 'binding' principle, tying the wage demands of all unions to increased labour force participation (see below).

Social Affairs minister De Koning took care of the human face of 'no-nonsense' government. Special measures were taken for the poor and families living on just one income at the level of the social minimum. As the most influential CDA power broker behind Lubbers, De Koning had convinced the Prime Minister, against the advice of DNB and the Finance ministry, not to follow

the Germans in the EMS currency realignment of 1983. The guilder devalued 2% against the D-mark—a decision that was soon regretted when financial markets demanded and extra risk premium. In March 1983, Dutch monetary authorities announced that henceforth the *gulden* was pegged to the D-mark. There would no longer be an independent exchange rate policy.

Helped by the initernational economic upswing, investments and jobs benefited from the recovery of profits in the second half of the decade. The reduction of working hours had an additional work-sharing effect, but the largest boost to jobs came from the rapid expansion of part-time jobs, mainly of married women and young people (Visser, 1999). The initial growth in part-time jobs during the early and mid-1980s did not result from policy changes, but rather from behavioural changes of women and employers. In the early 1980s, resisting the 36-hours working time campaign of the unions, employers presented part-time as the flexible and individual alternative. Dutch women used to withdraw from the labour market upon childbirth, but this was rapidly changing under the impact of better education, higher female wages, smaller families, and changing social norms. Faced with high risks of unemployment for themselves or for their husbands or partners, withdrawal from the labour market was more costly and risky. More women decided to stay and ask for reduced working hours instead of leaving. In the absence of day-care facilities, part-time work became the dominant 'coping' strategy of working women. Employers in sectors and firms with overcapacity saw part-time work as a welcome form of voluntary layoffs with little costs to themselves. In health, education and social services, but also in central and local government part-time employment was the least painful means to adjust to budget restrictions. Hiring of young people was often limited to entry jobs of 32 hours.

Lubbers' austerity policy paid off politically. In 1986 the centre-right coalition was re-elected with gains for his CDA party. Two governments of the same persuasion meant a clear break with the immobilism of the 1970s. Inflation decreased to almost zero in the mid-1980s and has disappeared from the country's worries, until recent. The strict exchange rate policy exerted disciplinary influence on wage developments, while, in turn, wage moderation enabled DNB to credibly stick to its non-inflationary policy. Low inflation allowed unions to forget about indexation. The new mix of macro-economic policy and wage setting also changed the institutional relations between unions, employers, and the state (Visser, 1998). The new pattern became: a central dialogue over a wide range of policy issues combined with sectoral wage bargaining, based on the primacy of industrial self-regulation. The role of the central organisations was confined to redirecting sectoral contracting towards tacit, economy-wide wage restraint and public regarding behaviour (van den Toren, 1996). These new principles have been recognized politically. The 1970 Wage Act was revised in 1986 and the possibility of intervention was narrowed to situations of extreme economic distress.

Since 1982 there has been no political intervention in wage setting. This is not to say the state has lost all leverage in Dutch wage setting. There is no unlimited *Tariffautonomie*, not even under the revised Wage Act (which has not been tested yet). Moreover, based on a 1937 law, the minister is authorized to declare collective bargaining agreements legally binding for all workers and employers in a certain branch of industry. This provision was routinely applied till the early 1990s but has since been used as a bargaining chip to obtain certain 'public regarding' objectives from wage negotiators, in particular lower entry wages, just above the statutory minimum wage, for people with low skills, little experience or a history of unemployment. The more independent position of the government, no longer depending on social partners for its own finances, has strengthened its position and this has in turn driven unions and employers closer to each other.

### *3.3. Trapped in a spiral of 'welfare without work'*

The second Lubbers-administration promised a further reduction of the deficit, not to increase taxes and social premiums, and lower unemployment to under 500,000 people. The new policy

challenge was to curtail the costs of social security and reduce the number of welfare recipients, which had continued to rise throughout the 1980s. Cost reduction did take place, mainly by freezing the minimum wage and all related benefits in nominal terms in 1983, followed by the 3% cut of 1984 and the de-linking of benefits from wages. The gap between average earnings of employed workers and the minimum wage increased by 12% between 1983 and 1989. Since the minimum wage is the basis for calculating state guaranteed minimum levels of all benefits, social assistance and basic old age pensions, this reduced the liabilities of the state. Youth minimum wages were reduced much more drastically (Salverda, 1996). At the same time, less adult workers remained at the minimum—the proportion of adult workers earning the minimum wage decreased from 10 to 3% between 1983 and 1995.

Under the increased competitive pressures of the 1980s, firms in the Dutch high-wage economy could only survive if they were able to increase labour productivity. Many embarked on a strategy of channelling less productive and expensive, mostly older, workers out of the labour market into unemployment or disability. Here there was a clear moral hazard, since the insurance costs were borne by all firms and, should funds run out, by the taxpayer. The rising insurance premiums resulted in higher social security contributions, while the wedge between total (wage and non-wage) labour costs and take-home pay increased. It engendered a vicious circle of employment destruction, of firms seeking to match rising costs by increasing productivity through layoffs, leading to higher costs, and so forth. The high average and marginal wedge created clear disincentives for workers to seek a job and threatened the continuation of wage restraint.

It became increasingly obvious that firms, with the complicity of social security administrators, were reducing slack while externalizing the costs, leading to an ever-growing volume of claimants. The so-called ‘system reforms’ in social security, implemented in 1987, had tightened eligibility and lowered guaranteed benefits from 80 to 70% of last-earned wages in case of unemployment, disability and sickness, but it had not altered the bipartite governance structure. After the reforms, Lubbers had promised ‘peace on the social security front’, but it was not to be. The contest over the rise in disability claimants could no longer be avoided and came to a head in 1991. When it came, Lubbers was fortunate enough to have traded his Liberal coalition partners for the Social Democrats, after a break in the old coalition (over environmental policy) and new elections in 1989.

Already in 1986 workers in the age group 55-64 who received a disability benefit outnumbered those with a job (Aarts and De Jong, 1992). These authors list four features that may explain the Dutch disability crisis (Aarts and De Jong, 1996). First, risks of disability were defined as social rather than occupational and the scheme did not make a distinction between different causes of disability. Second, until it was corrected in 1987 entitlement was based on an assessment of a worker's particular incapacity to find a job similar to his former job. Third, the administration of the sickness and disability schemes was separate; workers could first spend a year on sickness leave, almost unsupervised, and than move on to disability. Fourth, under collective agreements, most firms topped up sickness benefits to 100% of previous earnings and supplemented disability benefits to 100% during one year or longer. Workers drawing full-time disability pensions need not be available for the labour market.

The dismissal legislation under the 1945 Extraordinary Decree, meant to address the postwar chaos but still on the statute books, was another factor. The Decree had instituted preventive controls and required employers who wanted to end an employment contract to ask permission from the regional labour office director. Procedures could drag on for months, with uncertain outcome, and no permission could be legally granted when workers were sick or pregnant. The route through sickness and disability became the way of least resistance for many employers. Finally, administration and supervision of the system was in the hands of the social partners through so-called Industry Boards. These Boards were responsible for the medical service that assessed the degree of disability of workers. As it happened, there was extraordinary lack in

transparency of these assessments. All these factors conspired in a seemingly unstoppable rise in the number of claimants. A scheme that was expected to support no more than 200,000 people when it was inaugurated in 1967, had swelled to 900,000 benefits by 1990. Estimates at the time suggested that between 30 and 50% of all recipients were in fact partly of fully unemployed. The scheme also was a harsh welfare trap: once officially recognized as (partially) disabled, workers acquired a permanent labour market handicap, often combined with social isolation.

### *3.4 The political risks of welfare reform*

The third Lubbers administration (1989-94), now with the PvdA, led by ex-union leader and Wassenaar negotiator Kok as Finance Minister, began in an optimistic mood. Union decline had stopped and unions were regaining confidence, showing in a series of strikes in industry, transport, education and health services. For the first time in a decade, real wages increased (Visser, 1998). Economic recovery allowed for a partial restoration of the suspended 'index linking' of the minimum wage and benefits to wage developments. This had been one of PvdA's conditions in the coalition negotiations with CDA. Top civil servants at the Ministry of Social Affairs designed a new system of linking, which became operative in 1992. Index linking of minimum wages and benefits would henceforth depend on the volume of benefit claims in relation to employment measured by the so-called I/A (inactive/active) ratio. If this ratio exceeded a given reference level, fixed at its value (82.8) of 1990, the government would be entitled to suspend linking, fully or partially. In 1990, 1991 and 1992 linking was fully applied but in 1993, 1994 and the first half of 1995 linking was suspended since the I/A ratio had exceeded its reference value. In recent years the I/A ratio has rapidly decreased and linking has applied every year since 1995. The new conditional linking mechanism gave the unions, whose (ageing) members care much about linking of benefits to wages, a direct incentive to take account of the employment effects of wage bargaining.

Soon after the formation of the Lubbers-Kok cabinet in 1989 an unusual tripartite Common Policy Framework, with promises of growth, employment, tax relief and wage moderation, was agreed between the government and the social partners. With the unions employers did sign an agreement to create 60,000 additional jobs ethnic minorities, among whom unemployment was three times the national average. This agreement was not implemented, and hardly known among local employers or unions (Wilthagen and van Heertum-Lemmen, 1996). In 1994 the agreement was renewed, but employers made sure that no precise target was mentioned. Early 1991 the central employer withdrew their signature from the tripartite Policy Framework and stepped up their campaign for tax relief, lower non-wage labour costs and a cap on government spending. To drive their point home, employers decided to stay away from the customary spring meeting of the Foundation of Labour with core ministers from the Cabinet. Employers favoured one-to-one exchanges with the unions, or with the government, above tricky tripartism.

At around this time German unification boosted economic growth, but soon high interest rates dampened economic activity. Although the downturn of 1992-3 was not as bad as in other countries, the decline in unemployment was immediately halted and reversed. The government was preoccupied with the lack of a quick response from wage negotiators and prepared intervention on the basis of the 1986 law. The pressure worked and early 1993 the Foundation of Labour recommended a two months 'breathing space' in order to absorb the new facts of the international recession. Later in the year, after lengthy negotiations, a new agreement was reached, called 'A New Course', a true follow-up of Wassenaar, with more organized decentralisation and negotiated flexibility (Visser 1998). Employers gave up their blanket resistance against shorter working hours. Both parties agreed to work together in improving Holland's unfavourable employment/population ratio and recommended flexible working time patterns and part-time work as a solution. On the abolishment of remaining differences in rights

and fringe benefits between full-time and part-time workers there was a separate agreement. This was backed up in 1994 by legislation forbidding all discrimination on the basis of working hours. In the course of the third Lubbers-administration, the exchange logic behind organized wage restraint changed character. Increasingly wage moderation was matched by lower taxes for workers and social contributions for employers, made possible by improved public finances and a broader tax base. This was supported by the tax reform of 1990, which integrated taxes and social security charges, lowered the overall and highest rate, while limiting deductions. Since the national or basic social security contributions were integrated, the first band (37.3%) is mainly (32.3%) a social security charge, while the second (50%) and third (60%) bands are exclusively income taxes. (Payment for the three employee insurances—disability, sickness and unemployment—is collected collaterally, based on a fifty-fifty division between employees and employers.) By absorbing social security in the lowest band, and striking the deductibility of social contributions, the single largest item before 1990, the tax basis was broadened by almost two-thirds. The motive behind the 1990-tax reform was largely administrative, adopted to bring about a cost-neutral rationalisation of the Dutch tax system. However, since the reform was sugared by a tax break for most households, consumer spending surged by 4% in real terms, while private savings also picked up (De Kam 1996). As a consequence, the tax reform had unintended but highly favourable employment effects.

Lubbers I and II had exhausted the ‘price’ policy of bringing social expenditures under control through the freezing and lowering of benefits. PvdA opposed any further measures of this kind. The emphasis shifted therefore to a so-called ’volume’ policy aimed at reducing the number of social security recipients. Unavoidably, the political crisis of the Dutch welfare state came to revolve around disability pensions. The number of people receiving disability benefits seemed to approach the magic number of one million in a working age population of seven. In a well-played *cri de coeur*, in September 1990, Lubbers shocked viewers of the TV-evening news that the country was ‘sick’ and required ‘tough medication’. The next summer, after long agony, the government decided to restructure the sickness and disability programs. In response, the unions organized the largest postwar protest march in The Hague. This episode had far-reaching political consequences. The PvdA went through a very deep crisis and Kok, its leader, nearly resigned. Notwithstanding popular resistance, the reforms were enacted. They included a reduction of replacement rates for all workers under 50, including those who were already disabled (and could not take extra insurance). After some time, benefits would decrease to 70% of the statutory minimum wage plus an additional age-related allowance. Below the age of 50 those in the system would furthermore be subjected to new medical examinations, on the basis of stricter rules. In 1993, re-examination concerned 43,000 people under the age of 35, of whom 30% lost their benefit and 18% saw their benefit reduced (under pressure of Parliament, the regime has recently softened again). The legal requirement for partially disabled workers to accept alternative employment was tightened. Under the new sickness law of 1994 the first six weeks of wage continuation during sickness were directly charged to the employer (later this has been lengthened to the first year). In response to lower legal disability benefits, the unions negotiated extra-legal supplementary benefits in the collective agreements of 1995 and 1996 at the cost of the room for wage increases. As a result, the costs of sickness and disability have been internalized by the bargaining parties to a greater extent.

The 1994 elections were those of popular discontent. The Lubbers-Kok coalition was effectively voted out of power, losing 32 of its 103 seats in parliament, which is four short of a majority. This was as much as a political earthquake (Koole, 1995): no single Dutch coalition had ever lost so much support in one election. The extraordinary loss of CDA (from 54 to 34 seats) was caused by a leadership crisis and the untimely publication of a party document that future retrenchment might include a freeze of the Dutch basic pension scheme. Social democratic voters punished PvdA for its part in the attack on hard-won social rights. Ironically, however, PvdA, losing 12 of its 49 seats, became the largest party. A restored PvdA-CDA

coalition was now only possible with the help of the progressive Liberals (Democrats 66). This party convinced the historical enemies, PvdA and VVD, to form a coalition and form the first government since 1917 without a confessional party. The new 'purple' coalition did not slow down in its reform effort, but PvdA had a bottom-line condition for its co-operation: the level and duration of social benefits would not be tampered with. Kok had conceded that this position might have to be reviewed after two years, if developments in the public sector deficit, inactivity, and employment would turn out unfavourable. From this very defensive position, the party was entirely committed to the 'job, jobs and more jobs' approach as the only way out. This explains its support for reforms aiming at efficiency improvements, by means of the introduction of financial incentives through a partial re-privatisation of social risks and a managed liberalisation of social policy administration.

The common thread in many legislative changes in the system of social security is to place greater financial responsibility on employers and employees. This applies to the privatisation of the sickness benefits, the differentiation in invalidity benefit premiums, and the lengthening of reference days before workers receive a benefit under the new Unemployment Benefit Act. Under the new Disability Act of 1997 employers can 'opt out' and take full responsibility for the first five years of occupational disability, while legally obliged to pay at least 70% of last earnings. If they remain in the public system, they have to bear with the risk of rising costs if disability in the industry rises. This reform allows differentiation of employers' contributions and encourages firms to invest in health and safety at work. Employers can re-insure risks, but may have to pay higher premiums if rates are higher than average.

The welfare reforms of the 1990s were helped, politically, by the results of some alarming inquiries into the causes of the social security crisis. A Parliamentary Inquiry in 1993 revealed what was already common knowledge, namely that the social partners had made a 'very liberal use' of social security for purposes of industrial restructuring. The inquiry established that the Industrial Boards had no existential interest in getting people off welfare and that the social partners had all along known that the system was being abused. The government limited the self-governing autonomy of social partners and set up an independent Supervisory Board. A separate National Institute for Social Insurance was set up with responsibility for contracting the administration of social security out to privatized delivery agencies. Trade unions and employers associations have retained an advisory status only. A final string of measures concentrated on the introduction or intensification of activation obligations for the long-term unemployed, fortified by penalties since 1996. For young people entitlement to benefits was replaced by the entitlement to a job under the Youth Work Guarantee scheme. Single parents with children older than five (instead of twelve previously) must be prepared to take a part-time job. The standard for 'appropriate' work was broadened and benefit recipients are expected to accept jobs below their former job (and earnings) level. Municipal social services are required to draw up so-called reintegration plans and training programs, in collaboration with regional employment services. In line with requirements of the Luxembourg employment guidelines, the government is spending an extra Hfl. 500 Million for a so-called 'integral approach' according to which every unemployed worker will be made an job or education offer within the first year of unemployment

Unlike Austria and Belgium, Dutch citizens are entitled to a flat basic pubic pension when they reach the age of 65. In the face of a rapidly greying population, which is expected to reach a peak round 2020-30, nearly all parties have agreed to put aside extra tax revenue from the current growth success for a special fund to meet future obligations in this universal tier of the pension system. With respect to the obligatory occupational-based, earnings related second tier of Dutch pensions, unions and employers are quietly negotiating a change from a final to a middle wage system, and the replacement of collective early retirement schemes, financed from the wage sum ad in some industries adding up to 8%, by a funded time-saving system. Finally, as to the private non-compulsory tier, there is a move towards restricting the tax deductibility of

private equity plans, because they narrow the tax base. Because of its three-tiered make-up, the Dutch pension system appears better adapted to flexible, interrupted or part-time working careers than most continental European systems (Alber, 1998).

### *3.5. From fighting unemployment to increasing participation*

In the late 1980s, policy-makers became aware that the low level of labour market participation was the Achilles' heel of the extensive but passive Dutch system of social protection. In 1990 the Netherlands' Scientific Council for Government Policy proposed to break with the past and advocated a policy of maximizing the rate of labour market participation as the single most important labour market policy goal of any sustainable welfare state (WRR, 1990). Gradually, the message, though not the policy recommendation to lower the statutory minimum wage, was adopted by the government. In 1993 the social partners followed suit in their embrace of higher levels of participation in the New Course agreement (Visser and Hemerijck, 1997).

The new policy priority made its imprint on all kinds of policy initiatives, beginning with the I/A ratio as basis for benefit-wage linking. There was a new focus on active labour market policies, an underdeveloped area in postwar policy-making. The public employment service was reorganized. It had since long been run in a highly bureaucratic fashion from the Ministry, held a monopoly for job placement, was avoided by employers, and swamped by unemployed people with no chances on the open labour market. Its files were extremely polluted, with estimates that one-third of registered unemployment was not available for work or already working. Around 1980, the idea to involve the social partners was placed on the policy agenda. Minister De Koning believed that a tripartite organisation would condemn social partners and the government to mutual co-operation in the fight against unemployment. After lengthy preparations, the 1991 reform brought the service under tripartite control, financed by the government but run independently. There was also a strong element of devolution of responsibility to regional employment boards. A critical evaluation after four years led to another overhaul in 1996 and provided a policy window for issue-linkage between labour market and welfare policy. As a result of the strengthening of 'activating' measures in unemployment insurance and social assistance, municipalities and social insurance organisations have allocated a budget to buy placement and training activities from the employment service. From 2000 the employment service is expected to compete with private providers, like the temporary work agencies. Co-operation between social security organisations, the municipal assistance offices and the employment service is further enhanced by the 1998 Mobilisation of Unemployed Persons Act. They are expected to work together in one location, the new Centres for Work and Income. New government plans bring all insurances in one public service, whereas job placement services will be privatised, possibly within minimum requirements established by collective agreement. Unions, supported by employers, oppose these plans which would further reduce their involvement, but the Lib-Lab coalition appears determined to have its way.

Since the early 1990s, the Lubbers-Kok administration and the two purple coalitions-government had started to redress the balance between active and passive policies. Under the Youth Guarantee Plan and with the so-called 'Melkert-jobs' (named after the PvdA Minister of Social Affairs and Employment), permanent jobs in the public sector for unemployed youth and the long-term unemployed were created. These jobs are usually for 32 hours at a maximum of 120% of the hourly minimum wage. Additional job programs, based on these schemes, have been expanded and now absorb around 1.5% of total employment. The majority of these programs is carried out by the municipalities. With the introduction of the Jobseekers Integration Act local authorities are granted more resources to target projects for the long-term unemployed.

Next to job creation in the public sector, the government has introduced several kinds of employment subsidy schemes based on a reduction of social security contributions paid by employers. Subsidy schemes cover as many as one million workers. The first initiatives were directed at the long-term unemployed, women, ethnic minorities and low skilled groups. Because of a disappointing take-up, recent schemes cover all jobs with an hourly wage of up to 115% of the minimum wage. The majority of these jobs go to new entrants. Employment subsidies can add up to 25% of the annual wage. First evaluations of these schemes suggest that they accelerate employment creation and the reintegration of unemployed workers (SZW, 1998; NEI, 1999).

Labour market flexibility is an integral part of the new Dutch labour market policies. Legislation removing constraints on shop opening hours, business licenses, temporary job agencies, working time, and dismissal law consolidate this development. Following the 'New Course' agreement of 1993, unions and employers have in decentralized bargaining rounds concentrated on an exchange of shorter working hours, more leave arrangements and income stability throughout the year, in exchange for the annualisation of working hours, more possibilities for working in evenings or on Saturday, and lower overtime rates (Tijdens, 1998). The new Working Time Act of 1996, allowing negotiated contracts to deviate from legally defined maximum working hours or minimum rest periods, supports this trend. In 1993 the Foundation of Labour recommended that employers grant worker requests to work part-time unless there are compelling business reasons for rejection. A right to part-time work is currently under parliamentary review. Temporary work agencies provide for employment for over 200,000 person years in 1997. Almost half of the workers in a flexible job are under the age of 25; among adult workers the share of tenured contracts has been stable at 90% during the past ten years. In 1995 unions and employers signed the first collective agreement for temp workers, introducing a right of continued employment and pension insurance after four consecutive contracts or 24 months of service. It prepared the ground for the central agreement on 'Flexibility and Security' of 1996, which, in turn, paved the way for an overhaul of Dutch dismissal protection law in 1999. This 'flexicurity' law (Wilthagen, 1998) is a compromise, not just between employers and employees, but also within the unions between workers with and without stable jobs. A relaxation of statutory dismissal protection for regular employment contracts (more possibilities for negotiated termination-of-employment) is exchanged for an improvement of the rights of temporary workers and the introduction of a 'presumption of an employment relation' in the case of free lance work). Temporary employment agencies need no longer a licence, but the law assumes their responsibility as employer.

The incremental individualisation of the tax system since 1984, the improved possibilities to switch from full-time to part-time jobs, and the removal of all remaining elements of discrimination of the basis of working hours, have contributed to a 'normalisation' of part-time employment (Visser, 1999). The differences in hourly wages between full-time and part-time workers is 7% in the private sector, but much less in the public sector where almost half of all part-timers work. Dutch social security legislation is especially friendly for part-time employment, since the main principle for coverage, also for health insurance, is the employment contract, irrespective of hours worked (SZW, 1995). The current government has introduced a Framework Bill on Employment and Care to parliament, which is intended to harmonize different forms of leave and create a framework to save time or money for leave. Employers are lobbying hard to defeat this bill and instead propose to the unions to sign a Framework Agreement, with more sectoral flexibility. A tax reform, coined the Tax Plan of the 21st Century, has been proposed in September 1999. It includes lower tax rates on labour and capital, financed by the broadening and greening of the tax base. Capital asset taxes will be replaced by a fixed capital revenue tax. VAT will be raised, with the exemption of labour-intensive services, for which the VAT-rate will be lowered. The Central Planning Bureau expects the new tax system to considerably boost job growth, if there is wage restraint. But unions deny any relationship and

have already twice stepped up their demands for 2000, clearly responding to pressure from a tight labour market. Help from the tax side is still needed to bring more low-skilled workers into employment. But one might question whether under the present condition of a balanced budget and full employment it would not be wiser to increase public investment in education, technology, infrastructure, innovation and stress prevention, rather than heaping more money on house owners and consumers.

### 3.6 *The record: wage restrain, flexibility, part-time jobs, services, and welfare reform*

Since 1982 a new mix of macro-economic policy and wage setting emerged which generated a virtuous circle of price stability, fiscal consolidation, restored profitability, and strong (part-time) job creation in private services. Subsequently supported by welfare and labour market reform, this virtuous circle has had important positive feedback effects on female employment and domestic demand, which has led to a slow but solid decline in inactivity, without sacrificing basic social security. According to the Central Planning Bureau, wage moderation has been the single most important weapon in the Dutch adjustment strategy. CPB (1997) estimates that two-thirds of job growth between 1983 to 1996 should be attributed to wage moderation. Unit wage costs in 1996 were at the same level as they were in 1981. Over the same period they increased by 40% in Germany and 15% on average in the EU. The return to wage moderation contributed to job intensive job growth in three ways. First by restoring profitability, it created a necessary condition for investment and job growth. Second, by lowering the external exchange rate, it supported export growth and employment in the exposed sectors of the economy. Third, wage moderation kept more people on the payroll and had, in combination with lower taxes, a favourable effect on employment in domestic services. As a corollary of the shift to services, labour productivity per hour, although very high by European and American standards, increased less than in other countries.

Sectoral employment trends in the Netherlands went in almost opposite directions before and after 1984. In the 1970s the subsidized sector (health, education) and government employment witnessed the strongest growth, whereas private sector employment stagnated. Employment levels in industry fell steeply and employment growth in private services (trade and transport, financial and personnel services, hotels and restaurants) was faint. After 1984, job decline in industry and agriculture stopped. Employment growth is strongest in private services, 3% per year, four times as much as in the public and subsidized sector. The public sector absorbs only 13% of total employment, which is low in comparison with most European countries. The reason is that in the Netherlands health services and social welfare, are often organized by, formerly pillarized, ‘voluntary associations’ with support from public subsidies. Together with these semi-public activities, the public absorbs 25% total employment.

Next to wage restraint, labour time reduction and increased labour time flexibility have played a key role in job growth. Over time the policy preferences shifted from cross-the-board reductions in the working week towards the enhancement of part-time work and annualization of working time. Two-thirds of the jobs created since 1982 have been part-time jobs. The surge in part-time employment and the shift to services coincided with the rapid increase in labour force participation of women, from 29 to 60% between 1971 and 1996, the strongest rise in any OECD country. While the labour force increased with one-fifth between 1970 and 1997, the female labour force more than doubled (SCP, 1998).

By taking wage moderation, the proliferation of part-time work, the shift to services, and increased female participation together, the following picture emerges (Hartog, 1998). Between 1987 and 1996, value added in the total economy grew by 31%. However, employment volume (in hours) declined by 7% in the exposed sector and increased by 33% in the sheltered sector. Because private consumption is more service intensive, and services are more employment

intensive, job growth really took off in the service sector. Private consumption has been one of the major contributors to economic growth and was boosted by a 'feel good' factor related to the steady improvement in the labour market and rising housing prices (with most double earning families owning their house). Strong domestic growth has allowed the Netherlands to be relatively unaffected by the recession in Germany. The positive interaction effects between wage moderation, part-time work, the shift to services and increasing female participation have since the early 1990s been supported by social security reform and innovations in labour market policy. Transfers to households in GDP came down from 31% to 26% and the share of government expenditure in GDP declined from 62 to 52% from 1983 to 1998. In relative terms, related to the size of the labour force, there are fewer people on disability and sickness benefits. Today's discussions centre on the wisdom of further privatisation and incentives for employers to invest in the prevention of sickness and to reintegrate inactive workers. The reform of the employment service, the strengthening of activation requirements in social security, additional job programs in the public sector, wage subsidies to encourage employers hiring low skilled workers, tax reduction for those in work, negotiated flexibility in working hours, statutes and pensions, and policies to enhance the growth of part-time work, are all components of the Dutch job miracle. However remarkable that miracle is, it should be emphasized that inactivity, especially in the form of disability, is still high and that the present success is no more than a catching-up from a truly dismal situation in the recent past.

## 4. BELGIUM'S *SUR PLACE*

The international monetary crisis, the oil price shock and the international recession of the 1970s had a powerfully disturbing influence on the Belgian economy. During the recession unemployment doubled from 100,000 in mid-1974 to 228,000 two years later. By the end of the decade Belgium had the highest unemployment rate and the fastest increase in Europe but for Spain. Employment contracted by almost 6% between 1974 and 1983. In the private sector (without subsidized employment programs and self-employment) the decline was 15%. In manufacturing employment decreased by 29.8% and considering that average hours were reduced by 11%, we find that total labour input in manufacturing fell by 37.5%, which is a sharper contraction than in any other European country in this period.

Sneessens and Drèze (1986), from whom these figures are taken, present a broader picture of the Belgian economy, with time series data from 1962 to 1983 for the income share of labour, unemployment, inflation, balance of payments, and budget deficits. The striking feature of these data is the sharp break after 1973, indicating a deep transformation and severe imbalance of the Belgium economy. During the 1960s the Belgian economy had performed as well as its neighbours. In the early 1970s inflation and wage growth was above the trend in Germany or the Netherlands; unemployment was slightly higher; the overall employment/population rate was among the lowest in the OECD, as in the Netherlands; and the debt-output ratio was near the 60% limit which thirty years later would become the EMU norm. Having lost its colony in Africa in 1960, Belgium had found it difficult to adjust. Unlike the Netherlands, there was no compensation from gas resources. Thus, Belgium had less slack when it was confronted with the new realities of the 1970s.

Comparing the period 1968-1973 with 1973-1980 we find that GDP growth halved; export growth fell from 11 to 3% per year; inflation rose to 8%, whereas unemployment trebled over the course of six years. The public sector debt, fuelled by costly settlements of the linguistic conflict and steeply rising deficits in the social security funds, reached alarming proportions by

the end of the decade and would necessitate perennial austerity in the next. In 1981 the public deficit stood at -12.7% of GDP, which was the record in the OECD. Debt servicing alone had risen to almost 20% of government revenue. Deficit spending, which had helped to boost domestic demand in excess of supply in the 1970s, had as its counterpart an external deficit equivalent to -12% of GDP on a cumulative basis in 1981. This had to be financed by increased public borrowing, crowding out private investment. At the end of 1981 the net external liabilities were larger than the foreign exchange reserves of the Belgian National Bank (BNB). In that year the economy contracted with more than a full percentage point and unemployment, already high by the end of the 1970s, rose to 500,000 (10.2%) or 700.000 (16%) if people in various early retirement schemes are included. In sum, when the second oil crisis hit Belgium, its economic imbalances 'were more marked than in the majority of member countries and were tending to become self-perpetuating' (OECD, 1983:2).

### *4.1 The contradictory response of a hard currency and Keynesianism*

When the Bretton-Woods system collapsed, Belgium joined the 'snake'. It stayed in till the very end, despite the defection of France and other participants of the first hour. It did so for broadly the same reason as the Netherlands; with wage negotiators unwilling or unable to control cost push inflation, a hard currency policy was its main protection against imported inflation. As explained in the case of the Netherlands, this came at the tremendous cost of losing out on competitiveness in foreign markets. Jobs in the exposed sector were disappearing at an alarming rate. The index of unit labour costs in manufacturing, relative to the OECD average, shows that by 1975 Belgium had slipped to one of the worst positions. The so-called 'wage gap' or difference of wage costs between Belgium and its five main trading partners (Germany, France, the Netherlands, Italy and the UK), widened from 100 to 113 index points (1970=100) between 1972 and 1975 and further to 129 points in 1979 (Goubert and Heylen, 1999).

Exchange rate stability had long been a priority in Belgian monetary policy and was not contested by the unions. The experience of the 1949 devaluation had taught them that in a small economy, in which most goods are imported, devaluation hurts workers' purchasing power (Kurzer, 1993). Difficulties in obtaining voluntary wage restraint posed a dilemma to policy makers and all governments after 1974 were caught between the brake of a hard currency policy and the engine of a reflationary course for which there were insufficient resources (Jones, 1995). The immediate government response to the oil-crisis and the recession of 1974-75 had been to rescue industries in difficulties with subsidies, job creation in the public sector, and demand stimulating measures. Another response had been the reduction of labour supply, though a recruitment ban of foreign workers was largely ignored; early retirement of older workers; and an additional year of education for young people. It did not change much when in 1974 the Christian-Democrats shifted coalition partner, from left to right, and in 1977 returned to the Social Democrats. All governments till 1982 were wedded to a Keynesian approach.

Combining the civil service at the central and local level with the nationalized industries, public employment increased with 35.5% between 1970 and 1984, with an increase of 123,000 jobs in the direct aftermath of the 1974-75 recession and another expansion in 1978-79. The share of public in total employment rose from 23% in 1970 to 32% in 1982 (OECD, 1986). It was not enough. The recession accelerated the decline in the very industries that had been the mainstays of employment: steel, metal processing, chemicals, cars and transport equipment. Until 1975 heavy industry had absorbed redundant workers from labour-intensive industries such as textiles, clothing and leather, as well as coal mining, but this was now no longer the case. Overall, the employment ratio in manufacturing fell with more than four percentage points between 1973 and 1980, from 18.6 to14.3%. This contraction was twice as strong as in the Netherlands, not to speak of Austria where labour in industry was hoarded.

BNB estimated that total aid to business in the form of subsidies, capital transfers, loans and government equity investment, averaged 5.5% of GDP per year in the second half of the 1970s, peaking at 8.9% in 1982. This equalled 13% of government expenditure at the time and was unsustainable. In later years it would fall to around 7% (OECD, 1986). The largest item in the budget were subsidies to traditional sectors and large firms, in compensation for the hard currency policy, slowing down job losses as well as innovation. In the 1980s attempts were made to target government aid to starting firms and innovative projects in new technology. This coincided with the devolution of industrial policy to the regions, as part of the institutional reforms of 1980. However, the so-called 'national industries' (steel, coal, ceramics and glass, mainly located in Wallonia, and textiles and shipbuilding, mainly in Flanders) remained under the responsibility of the central government.

Before 1973 Belgium's main difficulties had been related to its outdated industrial structure and the shifting economic balance between the two regions. As the first industrial country on the continent, the country had inherited a large manufacturing base, concentrated in Wallonia. The decline in the demand for steel and coal began to hurt Wallonia as early as 1960. Post-war industrialisation programs and accommodating tax treaties had helped to attract foreign (mainly American) investment (oil and chemical industry near the coast and the port of Antwerp; light metal engineering and transport industry around Gent) and solve the age-old problem of underemployment in rural Flanders. With Belgian and foreign capital shifting its weight towards expanding Flanders, Wallonia fell behind. Unemployment had always been much higher in Flanders, but in 1970 unemployment in Wallonia (5.1%) was almost double the rate in Flanders (2.8%). By 1980 unemployment rates in both regions had slipped into double digits. However, unemployed has persisted in Wallonia and unemployment rates are currently three times higher than in Flanders.

### *4.2. Divided employers and strong unions*

In the 1970s wage negotiators failed to take account of the country's deteriorating external position (Goubert and Heylen, 1999) and Belgium ended the decade with the highest wage costs in manufacturing in the European Community (De Grauwe, 1994: 67). The unions continued to negotiate real wage gains in spite of the sharp rise in unemployment. This may be thought to reflect their continued strength (Hancké, 1993; Ebbinghaus and Visser, 1999) and is consistent with our hypothesis that Belgian trade union leaders continued to believe that wage restraint would not help but only depress demand and therefore aggravate the crisis.

With corporate profits under pressure, employers screamed for wage restraint and lower taxes every year since 1975. But they were internally divided and unable to attract the unions to a deal. In 1974 they signed what would turn out to be the last central agreement before long. Based on the 1944 Draft Agreement on Social Security and the 1954 Productivity Agreement, unions had committed themselves to the maintenance of social peace and the promotion of productivity in exchange for a share of workers in the proceeds of economic progress. In this spirit seven central agreements had been reached between 1960 and 1975. These had expanded the rights and benefits of workers, including old age pensions (1971), paid holidays (1960, 1963, 1966, 1973 and 1975), shorter working hours (1969, 1971 and 1973), national minimum wage (1975), equal pay (1975), as well as union representation rights in firms (1971). In this 'Golden Age of Planning and Growth' (Dancet, 1988: 217), parliaments had signed into law and governments had executed what the social partners wanted.

Until 1974, wage setting was entirely a matter of unions and employers, with no role for the government. Actual wage bargaining took place at the sectoral level and has been characterized as rather uncoordinated (Van Ruysseveldt and Visser, 1996; Vilrokx and Van Leemput, 1997). In comparison with Austria and the Netherlands, the role of the central organisations is limited.

Internally divided between sectors, regions and ideological currents, the central organisations carry little authority over their member organisations. This has proven to be a problem, in particular, in the Socialist union federation (FGTB), but also in the Belgian Federation of Employers (FBE) which faces a strong contender in a Flemish organization (VEV). The central organisations do meet in direct consultation in the National Labour Council (CNT) where they have the right, since 1968, to negotiate binding agreements. At the sectoral level, collective agreements are negotiated in some 130 parity commissions which meet under an independent chairperson and are assigned the task to negotiate (binding) agreements, settle and prevent disputes, and advice the government. With the main exception of the chemical industry, company bargaining is secondary and mainly concerned with non-wage issues.

In 1975 the central employers' organisation pulled the brake and recommended a small wage increase, but according to FBE chairman Puellinx his advice went unheeded and most sectors negotiated a real wage increase of 5% or more (interview, Swav, 1995: 5). Similar attempts in later years failed and until 1982 gross wages and wage costs outpaced productivity growth by a wide margin, with the implication that unit labour costs increased (see Table 6 for a comparison with the Netherlands). The result of uncoordinated wage bargaining was, as in a prisoners dilemma, a higher cost for society in the form of rising unemployment and social security expenditure. The bargaining parties maintain an interest in demanding social protection (unions) and subsidies (firms), the costs of which are shouldered by the community at large. Unavoidably, this development led to the state involvement in wage bargaining and the change from bipartism to tripartism (Slomp, 1983). However, until 1981 all attempts to encourage unions and employers to accept restraint failed. Each side had a sticking point: employers refused to discuss working time reduction, unions ruled out real wage restraint, and governments could not afford to give up the strong currency (De Swert, 1989). But the government was not in a position to stand aside. It needed wage restraint, if only to limit the rising claims and costs of social security and the increasing deficit in public spending. After 1981 the government took an authoritarian line and from 1982 to 1986 free wage setting through negotiations between unions and employers was suspended.

The central organisations not only lacked control over their members, they also disagreed over policies. As in many other European countries, Belgium witnessed a period of worker militancy and radicalisation of union demands after 1968 (Molitor, 1978) and Belgian employers felt ideologically under attack (Moden and Slover, 1980). With the slow-down of economic growth, it became less easy to find compromise solutions. In 1976 *Fabrimetal*, FBE's powerful affiliate in the steel and metal industry, alarmed by the rapid deterioration of the competitive position of its members, demanded the abolishment of the indexation system. Established in the immediate postwar years, this system guaranteed that wages were fully adjusted to price increases, making wages inflation-proof. The technique was that each index point rise in the consumer price index was translated, after two months, in a similar rise in wages. Coverage was nearly complete and, following an earlier agreement, the system was in 1975 extended to the national minimum wage and social benefits. The attack of *Fabrimetal* received insufficiently backing in other sectors and under pressure of strikes employers were forced to retreat. Indexation became a 'holy cow' and remained a sticking point in Belgian industrial relations during the next decades. The arguments in favour or against indexation and the deleterious effects on bargaining discussed in the preceding section on the Netherlands apply with equal force to Belgium. However, unlike Dutch (and later Italian) union leaders, Belgian union leaders remained steadfast in their defence. Their behaviour contradicts the hypothesis that in a continued low inflation environment union leaders loose interest in an automatic cost-of-living adjustment wage since it narrows their role and autonomy in collective bargaining (Braun, 1976). The unions countered employers' pressure for wage restraint with demands for working-time reduction. In 1976 Belgian unions, beginning in the troubled steel industry, were the first in Europe to raise the demand for shorter working hours as a work sharing measure, but negotiations were fruitless.

**Table 6: Average annual growth of real (gross) wages, inflation and productivity**

| | real (gross) wage growth | | productivity growth | | effect of inflation | |
|---|---|---|---|---|---|---|
| | Belgium | Netherlands | Belgium | Netherlands | Belgium | Netherlands |
| 1971-1982 | 4.14 | 2.72 | 2.80 | 2.28 | 1.36 | 0.44 |
| 1983-1985 | -0.75 | -0.91 | 1.35 | 2.53 | -2.09 | -3.44 |
| 1985-1989 | 0.70 | 0.70 | 2.02 | 0.79 | -1.33 | -0.11 |
| 1990-1995 | 2.20 | 0.31 | 1.73 | 0.72 | 0.46 | -0.43 |

Source: Conseil Central Economique, report on the Belgian economy in 1997.

Note: real (gross) wage is calculated as the sum of all (nominal) compensations to wage and salary earners divided by the total number of wage and salary earners in employment, deflated by the consumer price index. Labour productivity is calculated per person (rather than per hour, explaining the low figure after 1985 in the Netherlands, due to part-time employment). The effect of inflation can be seen as the difference between productivity and wage growth.

The first of many state interventions in wage bargaining came at the end of 1976 when Belgian's outgoing centre-right government imposed a 'special levy' of 50% on all contractual pay increases above indexation in order to finance a special fund for older unemployed worker who were allowed to stay outside the labour market on a transitory pension till legal retirement age. This provoked a national strike, jointly organized by the socialist and Christian unions, the first-ever strike of the latter against the government (with their own ministers). The incoming centre-left government boosted public sector employment and tried to gain unions and private sector employers for a package deal based on wage restraint, working time reduction and job targets equivalent to 2% of the workforce. This attempt at political exchange failed. Unions wanted more assurances that there would be additional job, whereas employers rejected the targets as 'bad therapy' and interference with management. When the government dropped the targets and offered a voluntary scheme for subsidized working-time reduction, employers in some sectors, mainly those with overcapacity, did accept negotiations over working-time reduction. The moderating effect on wages was small. The unions were disappointed that the job targets were dropped and the subsidies lowered the employers' resistance to wage demands.

### *4.3 The 1980s: International pressure and recovery*

In the early 1980s, Belgium earned 'the dubious distinction of being the first and only Member State to receive an official recommendation of the European Commission to address its growing public deficits and rapidly growing wages' (Kurzer, 1998: 118). At the European Summit of 1980, Belgium was 'advised in strong terms' to modify its 'prejudicial system of wage indexation if it wants to stay in the EMS' (Dancet, 1988: 211). Impressed, Prime Minister Martens proposed a temporary suspension of indexation, apparently without consulting his socialist coalition partners, whose ministers resigned. The next government, again with the socialists, asked special powers of parliament and only 48 hours before a wage stop would have taken effect, unions and employers agreed to seek voluntary restraint, packaged with some working-time reduction for 1981-82. Unlike the Dutch agreement of Wassenaar, this agreement was not the dawn of a new era in industrial relations. It was too obvious a *dictate*. Union leaders had intellectually not come around to the idea that profitability and competitiveness had to rise in order to prevent further job losses, as had Dutch union leaders by this time. Moreover, in addition to the low trust of Belgian negotiators in each other, there was no stable government that might have protected a compromise between the social partners against defection or abuse.

Indeed, within weeks the government fell (over the federalisation issue), provoking the fourth crisis in two years. In an unusual speech King Baudouin reminded politicians that time had come 'to put our differences aside' and 'give priority to survival', as one 'would do if we were at war' (…) 'war for the preservation of our economy' (Deweerdt and Smits, 1982: 262). But the next government did no more than solve another piece in the federalisation puzzle and postpone what Belgian employers now called 'the evident decision', by which they meant the suspension of wage indexation. Instead, the government bought time and offered employers a flat-rate reduction in social security contributions for manual workers in manufacturing firms in difficulty (*Maribel*, law of 29 June 1981).

The general elections of 1981 resulted in losses for the Christian-Democrats in Flanders and gains for the Liberals. Forming his fifth Cabinet, CVP-leader Martens chose the Liberals as his coalition partner. Despite its narrow majority in Parliament, this coalition would stay in office the full four years and was continued unchanged after the elections of 1985. Martens V more or less ruled by decree, seeking special enabling powers from Parliament in an annual vote of confidence. This silenced not only the Socialist opposition but also its internal critics, especially from the Christian union wing. This 'less democracy for a better economy' approach (Smits, 1983) was defended by Martens as 'an unavoidable step in the recovery of our country' (Bastian, 1994: 92). Not only Parliament but also the collective wage negotiators were placed in 'preventive custody' (Vilrokx and Van Leemput, 1997: 336-7).

The recovery began with a large devaluation of the *franc*. Early 1982, after negotiations within IMF and Ecofin, a 8,5% devaluation was obtained, the largest since the start of the EMS (Gross and Thygesen, 1994: 76). The liberals had wanted more, the unions, like the *Bundesbank*, less (Kurzer, 1993). Devaluation could only restore the competitiveness of Belgian firms if combined with full-proof wage restraint. Hence, a standstill on wages (till May 1982) and a suspension of indexation for the entire year were crucial. Martens and his aides had secretly negotiated the recovery plan with the veteran leader of the Christian workers' association who used his influence to assure co-operation from the Christian unions. They consented on condition that suspension of indexation would be temporary and special income protection was given to low-paid workers and large families. The Socialist unions were left in the dark, but their strikes altered nothing to government policy. During the next four years, until the end of 1986, the government decreed that three index jumps, each amounting to a price increase of 2%, would not be translated in wages and that any wage increase above inflation was prohibited. In combination with the devaluation, these draconian measures did indeed lead to a sharp turnaround in competitiveness. Real wages fell between 1982 and 1986, and all productivity gains were captured by firms, leading to a sharp decline in labours' share in enterprise income. However, at the same time the government raised the employers' contributions for social security in otder to meet its second objective of fiscal consolidation. Hence, non-wage labour costs decreased much less than wages and the wedge between labour costs and take-home pay rose sharply. Since the government had agreed to exempt minimum wages and heads of (large) families from its measures, or offer compensation, the distance between minimum and average wages narrowed and the overall wage structure compressed.

There are similarities, in background and content, between the Belgium recovery plan of 1982 and the 'no nonsense' approach which started later in the same year in the Netherlands. Both were responses to a very severe crisis, implemented by centre-right governments with a strong electorate mandate for the conservative Liberals. In both countries, as in Germany or in Britain two years earlier, the Social Democrats had exhausted themselves as government partners by the failure to tame or convince the unions (as well as by their antagonism against permitting a new generation of nuclear weapons on Dutch and Belgian soil). In both countries the recovery plans aimed at the restoration of private sector profitability, fiscal consolidation and a slow-down if not reversal of the upward trend in unemployment through job-sharing. The overall package was deflationary in both countries and at first increased unemployment. It implied a shift of incomes

from households to enterprises, showing in a fall in labours' share in net national income. The main difference, however, was that in the Netherlands recovery was consolidated by a major agreement between the unions and the employers. As was argued in the preceding part on the Netherlands, this allowed the government to concentrate on fiscal consolidation and uncouple public sector pay from private sector wage negotiations. In Belgium there was no such agreement, leaving the government in a more vulnerable position, with many risks of implementation failure and political horse-trading.

The choices of the Belgian government were constrained by the fact that it started the decade with a huge public debt and that social security costs had risen spectacularly. There was no money for lowering taxes on employers or workers, or boost consumer demand through tax reform. While the cost crisis in social security was probably more severe, the austerity measures were rather piecemeal and drawn out over a longer period than in the Netherlands, possibly because the opposition of the more powerful Belgian unions and within the Christian-Democratic party was stronger. Belgian social security for workers is contributions-based, but premiums covered in 1983 only 62% of total expenditure, against 84% in 1970 (Peeters, 1989: 202). Many funds had fallen into dept. The deficit in social security, combining all programs, had increased nearly tenfold, from 26 Belgian francs in 1970 to 254 billion francs in 1980, with the rise in unemployment benefits as the largest contributing factor. The number of unemployed receiving full compensation from the insurance funds had trebled between 1974 and 1980, expenditure on unemployment rose from 0.7% of GNP in 1970 to 5% in 1985. As part of a first austerity package, unemployment insurance entitlements had been differentiated between principle breadwinners with dependent families, single households and people earning a second household income in 1980. For the latter two categories, benefits were lowered and phased out earlier. In later reforms, an extended 'waiting time' of 150 days applies to school-leavers before they may claim a reduced benefit. After 1982 benefits did no longer follow wage increases (a principle only introduced in 1975), but breadwinners and large families received compensation.

Another cost explosion concerned the various early retirement schemes. Faced with the explosive growth in youth unemployment, which had risen to 25% in 1980, and the structural crisis in coal mining, steel, ceramics, textile and shipbuilding, Belgian governments believed that they had no choice but encourage the pre-pensioning of workers. It was, moreover, the only policy response on which there was agreement between the social partners (Bastian, 1994). The appeal of this approach shows in the sharp fall of the employment ratio of older males, between age 60 and 65, from just over 60% in 1970 to 32% in 1981. By 1983, the first year for which we have internationally comparable data, the employment/population ratio in this age group was lower in Belgium than in all other countries except Luxembourg. Older workers received a pre-pension until legal retirement age in case of unemployment and public subsidies were available for early retirement in case of replacement by a young worker. The costs were initially fully borne by public funds, like the unemployment insurance fund, but after 1982 the government introduced special levies.

Work sharing was the third plank of the 1982 recovery plan. Under the so-called 5+3+3 operation, initiated in 1982, unions and employers were encouraged to negotiate a 5% reduction in working hours in exchange for a 3% wage sacrifice and a 3% increase in employment or, failing that, an obligatory employer contribution to the National Employment Fund. Attempts to negotiate a central agreement along these lines came to naught. Employers, once assured of government-imposed wage restraint, needed to make no further concessions. Unions felt that they had been robbed of an instrument—wage pressure—to wrest concessions from employers on labour time reduction and job creation. Yet, in sectors and firms with overcapacity employers and unions did reach agreement for about 1,3 of the two million employees in the private sector (Béguin, 1985: 37). With an average working time reduction of 1.4% and a net employment effect of 52,100 jobs (Werner and Konig, 1987: 62) about half of the government's target was reached. The Federal Minister of Labour, defended state intervention on the ground that he had

no choice but 'oblige the labour market organisations to negotiate amidst a web of constraints, which both sides had refused in previous years' (Hansenne, 1985: 56). This approach was also applied in the so-called 'Hansenne working-time experiments', in which the state offered to suspend legal norms on maximum daily or weekly hours and overtime rules, if firms could show positive effects on investment and employment, and signed an agreement with the unions and the Ministry. 55 plant agreements of this kind were signed between 1983 and 1986, in total affecting 26,000 employees (Denys et al., 1985), nearly all in large manufacturing firms, including Siemens, Phillips, Samsonite, and General Motors, all of which were interested in increased flexibility and located in Flanders. The Socialist unions in Wallonia would have nothing of it (Bastian, 1994: 101; Colpaert, 1987: 41).

### *4.4. Safeguarding EMU participation*

In 1990 the monetary authorities, anxious to quell the occasional speculative frenzies against the *franc*, promised to preserve the parity with the DM in the event of a realignment and BNB gained the same degree of independence as German and Dutch Central Banks. Having signed the Maastricht Treaty on Economic and Monetary Union, Belgium set itself the objective to belong to the first group of EMU members. It had much to gain from borrowing the reputation of the DM (Dyson, 1994: 207) and as a transit economy it had much to loose should it be excluded. But on at least two major indicators—the public sector deficit and the debt-output ratio—Belgium was far off the target.

With the entrance of the Socialists in Martens' seventh cabinet (1988-1991), fiscal control had been relaxed and the link between price indexation, wages and benefits restored. From 1987 to 1993 wage bargaining was again in the hands of unions and employers, albeit under a 'shadow of hierarchy', as defined by the 1989 Law on Safeguarding Competitiveness of Enterprises. This law authorized the government to intervene, *ex post*, if wages in Belgium had risen faster than the average trend among its five major trading partners (Michel, 1994). Twice every year, the *Conseil Central Economique* (CCE), with bipartite representation of unions and employers, and co-opted economic experts, issues a report on the state of the economy. If it sees fit, it may recommend wage guidelines and other measures. The balance sheet of this period of limited 'free' wage bargaining (1987-1993) is mixed. The central organisations were able to conclude (biennial) central agreements, but 'devoid of content and largely dictated by government' (Vilrokx and Van Leemput 1997: 341). The fact of the matter is that these agreement did not uncouple, or differentiate, collective bargaining in different sectors, as was by now the case in the Netherlands (and would further increase in the 1990s) and had always been the case, under strict leadership, in Austria. In Belgium, instead, wages in high productivity sectors, like manufacturing, kept setting the norm for wage increases in low productivity sectors, like domestic services. By their very nature, statutory interventions are unable to differentiate by sector, because of asymmetrical information and monitoring problems (the Dutch had tried and miserably failed in the early 1960s). Between 1987 and 1989 and again in 1993 gross wage increases did stay within the boundaries of overall productivity growth, but in the other years the opposite was true. In all years wage rises in services exceeded the much lower productivity gains in both services (around four times lower than in manufacturing according to figures of the Belgian Planning Bureau). Moreover, the responsiveness to unemployment and to economic shocks was limited. Regressions over the full period from 1970 to 1993 showed that in the Belgium case a rise in unemployment with 2% is needed to obtain a 1% decline in real wages (less than half the elasticity in for instance Austria) (Heylen and Van Poeck, 1995).

In the 1990s the old competitiveness problem resurfaced. One reason was that Belgium suffered more from the EMS troubles of 1992 and 1993 than Austria or the Netherlands. The new round of federalisation in 1988 had not encouraged 'the kind of fiscal behaviour associated

with restricted monetarism' (Kurzer, 1997: 120). International confidence in the franc remained low (in 1993 BNB had to accept wider margins between *franc* and D-mark). The other cause was wage growth. The CCE report for 1994 stated that Belgium had again developed a handicap of 6% against its trading partners. This figure was disputed by the unions, who called the statistics unreliable and blamed the recession on the deflationary policies of the *Bundesbank* and on the restrictive EMU membership criteria agreed in Maastricht (Serroyen and Delcroix, 1996: 36). Formalized in its so-called EMU convergence plan of 1992, the government had in 1992 ushered in a fiscal consolidation package, aiming at reducing the deficit from 7% to 3% of GDP by 1997 (OECD, 1995: 7). Later a 3% EMU tax surcharge was introduced (abolished in 1999). During the EMS crisis a group of prominent Belgian economists called for unpegging the frank, the abolishment of indexation and an overhaul of the social security system which they described as 'wasteful' and 'inefficient' (Kurzer, 1997: 120). The proposal was hardly echoed in the press. Some unions might have favoured a softer currency but not at the price of giving up indexation or lowering social security. Employers, choking under high costs, might have favoured a softer franc, but they did not trust that unions would give up on indexation and deliver restraint. Instead, their primary objective was lower government expenditure, taxes and social security charges. BNB was adamant in its defence of a *franc fort*; devaluation would mean higher imported inflation, diminished fiscal discipline, a rising public debt and probably goodbye to EMU-membership.

In comparison to the Netherlands where early 1993 a temporary wage stop was implemented, followed by a new central agreement later in the same year, Belgian wage negotiators were slow to adjust. The renewed Christian-Socialist coalition, led by CVP's new leader Dehaene (1992-1995), was unable to coax the unions into signing a similar pact for competitiveness and employment. Alarmed by sharply rising unemployment, the government had proposed a 'Global Pact' early in 1993. On the basis of a grim report on the Belgian economy, prepared under guidance of the National Bank, negotiations started in October. Infuriated by the proposal to trim the cost-of-living index, the socialist federation FGTB, under pressure of its powerful affiliates, walked out (Van Ruysseveldt and Visser 1996: 215; Wauters, 1997). The government, including its socialist ministers, went ahead and excluded tobacco, alcohol, petrol and diesel fuel from the calculation of the cost-of-living index. The new so-called 'health index' lowered the adjustment of wages and benefits projected for 1994 and 1995 by 1.3 percentage point (with a projected 2% annual rate of inflation) (OECD, 1995: 10). With the government's Global Plan becoming law in 1994 the eight-year interlude of limited freedom in wage setting had ended (Blaise and Beaupain, 1995). From now, wage bargainers were placed under 'house arrest' (Vilrockx and Van Leemput, 1997). Nominal wage increases, beyond the watered down price indexation, remained banned until the end of 1996.

The second Dehaene government (1995-1999), again a Christian-Socialist coalition, started with proposing a 'Pact for the Future of Employment', in pursuit of three objectives: to halve the current unemployment level of 12% by 2002; improve the sluggish rate of GDP growth (1,5-2%); and secure the 3% budget deficit target required for EMU membership. The new government was under pressure from Europe and the regions. In Flanders, in particular, employers and the regional government were showing impatience with the national government. Consultations over the Future Pact continued until April 1996 when VEB reached a draft agreement with the unions. Its content was, once again, wage moderation; a legal maximum working week of 39 hours in 1998; improved rights for leave of absence without pay, part-time retirement at age 58 and full-time retirement at age 60; annualisation of working-time; and lowering of employers' social security contributions through the expansion of the Maribel subsidy schemes. The agreement failed, however, when the socialist union federation FGTB was unable to gain approval from its affiliates. The leadership of the Christian federation ACV slipped through with a slight majority (Van Ruysseveldt and Visser, 1996: 217).

The government went ahead, selectively borrowing from the failed agreement. The central

wage standard was given a legal status with a new framework law. This 1996 Law on Safeguarding the Competitiveness of Enterprises proscribes that wage increase in Belgium must remain below the *average* wage increases of its three neighbours Germany, France and the Netherlands. This was a clear tightening of the old law of 1989, which had entitled the government to intervene *ex post*. The new law introduced an *ex ante* maximum wage norm based on predicted wage increases in Germany, France and the Netherlands. Under the law, industries and firms are punishable if they exceed the norm; they may settle for lower wage increases, for example, in exchange for extra job measures. The (revised) indexation mechanism remained in place. The Act also stipulates that multi-industrial bargaining must take place every two years, on the basis of the CCE's technical report, and lead to an agreement on the precise margin for sectoral bargaining and additional job creation or working time matters. If no agreement is reached, as was the case in 1996, the government unilaterally sets the margin. For 1997 and 1998 it specified a maximum increase of 6.1% over two years, including a predicted 3.6% rise in consumer prices, 1% seniority related wage increases and a real across-the-board improvement of 0.75% per year (Vilrokx and Van Leemput, 1997: 339-40). The second round of bargaining, for 1999-2000, did produce an agreement. This was eased by the government's decision to reduce social security contributions by 108 billion francs (2,5 million Euro) in five years and bring social charges down to the average level of the three neighbours. FBE was under pressure of its Flemish regional partner, which had announced to 'go alone' should no national agreement be reached. This time the federal leadership of the unions gained consent from its member unions. The deal itself was complex and linked the future reduction in social contributions to compliance with the wage norm or, failing that, extra spending on vocational training. Companies and sectors paying above the norm will not be penalized (as they should have been if exceeding the norm in 1997 and 1998) if they can show that there are no negative employment effects. Not only was this extremely difficult to monitor, but it requires a kind of sectoral, regional and company data on investment and employment which is not available.

### *4.5. Lacklustre growth in the 1990s*

In the 1990s Belgium exemplified Europe's main illness: high structural unemployment and the lack of productivity and employment growth in private services. As elsewhere, the problem was magnified by the slow-down in international economic growth and the restrictive policies in the run-up to EMU. But this cannot explain the difference with the two other countries discussed in this chapter. The causes of Belgium's low employment growth are probably a cluster of factors relating to problematic wage setting, a high tax and social security wedge, various unemployment traps, inefficient active labour market policies, to mention only some factors (Elmeskov et al.,1998; Goubert and Heylen, 1999). Past culprits were an ageing industrial structure, full wage indexation and excessive real wage growth. Once unemployment was high, and persisted, social policies and labour market measures had to be expensive, even after various retrenchments. The weak social consensus and capacity for compromise delayed and weakened responses. The job leak due to deteriorating international competitiveness was only mended by placing wage negotiators under direct government control. But in international comparisons of wage costs, Belgium still comes up very high, second only to Germany. The OECD (1997: 1) maintains that 'improving the wage formation process remains a largely unresolved issue'. This is also the view of the government's own advisors, for instance of the newly established High Council for Employment whose 1998 report on the matter was however largely ignored.

Pattern bargaining has negative consequences, in particular, when productivity trends divergence. In Belgium, differences in productivity gains across sectors are very large; from 1970 to 1996 average annual productivity gains were 4.7% in manufacturing industry, against 1.0% in services (BPB, 1998: 108), a gap which is almost twice in excess of the European

average. If wages exceed the very small productivity margin, and wage bargaining is in real terms, profits and investments will decline. Consequently, job losses in manufacturing (between 1970 ad 1994: -463,000), were hardly compensated by job increases in services (+682,000, of which only +114,000 in non-market services). With further decline in agriculture, energy and construction, overall growth was just +35,000 jobs.

Another reason for concern is the compressed wage structure, especially at the lower end, with little variation across sectors, regions and skill levels, despite very large differences in unemployment, labour demand or productivity. Together with the strong bias towards passive labour market policies and earnings-compensating role of social security, this may explain why job turnover and labour mobility in Belgium is low, especially in Wallionia (De Grauwe 1998; Goubert and Heylen 1999; Marx 1998). There are a number of unemployment traps, related to the length rather than to the level of unemployment benefits. Net replacement rates for single parents and breadwinners, measured against the minimum wage for full-time workers, are estimated at 107% and 91% respectively. For part-time workers at 50% of the minimum wage, net replacement rates vary around 90% and 96% for breadwinners and unemployed spouses (Cantillon and Thirion, 1997). Married women receive a small unemployment benefit, which often serves as a second income in the family. They have little monetary incentive to accept a job if it is not full-time This applies particularly to low-income families. Moreover, the strong family-bias in unemployment benefits discourages spouses of unemployed workers to seek or hold on to part-time jobs. Already in 1975 the female rate was twice the male unemployment rate and in 1980 the ratio had increased to 3:1. This was partly determined by faster labour force growth of women, but unlimited unemployment insurance is another part of the story. In the 1990s the female/male disadvantage returned to a ratio of 2:1, partly because of withdrawal from the labour market. Since 1987 administrators were entitled to suspend unemployment benefits of second earners if unemployment spells were exceptionally long (i.e., 1,5 to 2 times the average of the industry or occupation).

Effective minimum wages, as defined by collective agreements, lie 20-30% above the statutory minimum. This would suggest that unemployment traps may be not as bad as they seem (Jadot, 1988). However, the high level of wages at the lower end of the Belgian labour market, combined with a high level of wage costs and low profits, discourages job creation in services. This disadvantages workers with low levels of education, those with long unemployment spells, or women who try to re-enter the labour market. For exactly this reason, Dutch governments since 1993 have successfully exerted pressure on unions and employers to lower negotiated minimum wage levels, together with wage cost subsidies for the low paid.

Wage cost subsidies to employers have remained the only answer, but until recent they were only targeted to industry. During the 1992-93 EMS crisis there was a rapid expansion, from 15 billion BEF in 1993 to 60 billion BEF in 1996 (there are roughly forty *francs* to the *Euro*). As in the original *Maribel* scheme of 1981, subsidies were intended to compensate exporting firms for the hard currency policy and to slow-down the decline of manual work in manufacturing. On precisely these grounds the European Commission repeatedly criticized the subsidies as a distortion of competition, since they were not open to all firms. In response, the program was in 1997 widened and offers a reduction of social contributions to all private firms, including services, proportionate to 'labour intensity'. The revised Maribel scheme is valid until the year 2000 and applies to about 770,000 workers, against 431,000 in the old program. Unions criticise the subsidy as a handout to employers (Serroyen and Delcroix, 1996: 37). But the proposal of Socialist ministers to make the subsidies contingent on explicit job targets was not implemented. Studies of the Belgian Planning Bureau suggest that a selective subsidy program, targeting workers with low earnings, would create more jobs but are costlier and difficult to monitor (Bossier and Masure, 1995; CNT, 1998). In 1995 the federal government has however phased in an additional 'low earnings' subsidy scheme, applying to 782,000 workers at or around the minimum wage, whose social security charges are lowered by between 2 and 12% of total wage

costs. In 1996, 36% of total expenditure on tax- and charge-reducing subsidies went to Maribel, 24% to the low earnings scheme and 20% to special job creation plans for the long-term unemployed (De Lathouer, 1999: 199). The remainder was set aside for contingent plans, negotiable with trade unions and employers.

As was mentioned in the introduction, Belgium spends more on 'active' labour market policies than either Austria or the Netherlands. Total expenditure nearly doubled from 64 billion BEF in 1985 to 112 billion BEF in 1994. Against the background of the rise of long-term unemployment to 6% of the active labour force, the increase is less impressive and the effectiveness of policies may be questioned. Placement offices and employment services are highly overburdened and in 1990 it took on average 20 months before an employed person was contacted by a case officer (OECD, 1994). Non-participation in job-placement programs is rarely penalized. Only 20% of total expenditure concerns training and education, and just 6% of the unemployed participate in training or work experience programs (De Lathouer, 1999: 200). Subsidies absorb most costs. Although there is perhaps no second government in Europe with so many job plans, many quite creative, Belgium's top civil servant in the Ministry of Labour described in a recent policy review his government's job policies as 'plainly unrealistic' (Jadot 1998).

Many of the schemes are along the lines of the 5+3+3 schemes of the early 1980s. The government makes subsidies available, or lifts certain legal restrictions on work or working-time regulation, if employers create extra jobs, and unions sign up to extra wage restraint and greater flexibility. Some of these schemes are specifically designed for young workers, the long-term unemployed, small firms or the non-profit sector of charitable work. The take-up of subsidy schemes, to be negotiated under company or plant level agreements, has been disappointing (Serroyen and Delcroix 1996: 43) and control over implementation is extremely difficult. A possible explanation is that Belgian unions and employers are not ready for the kind of decentralized bargaining which is required (Vilrokx and Van Leemput, 1997: 341). Internally divided between their regional wings, Belgian employers associations fear the strength of the union delegate system at the local level and the militant stance of the union rank-and-file in Wallonia. The Socialist union confederation dislikes decentralisation for opposite reasons; left to their own devices, its Flanders' representatives would go along with even more flexibility than they (and the Christian unions) presently do, whereas its Wallonian representatives would probably accept even less change. Sectoral plans, negotiated under a central agreement of 1994, have been more numerous but they mainly focused on early retirement. The agreement once again widened the possibilities of early retirement from age 58 to 55, under certain conditions. Many agreements allow workers with a minimum of 33 years of contribution to leave at age 55 and nearly all permit older workers to stay half-time and receive a supplementary unemployment benefit until they reach the legal retirement age of 65.

Part-time employment has remained unpopular with the unions. Unlike the Netherlands, it has not been or become the dominant choice of working mothers. The full-time employment/population ratio of Belgian women is almost double that of the Netherlands, whereas the part-time employment/population ratio is nearly three times lower (Visser, 1999). Historically, a much larger number of Belgian married women continued to work full-time and child care facilities, especially for very young children, have generally been available on a much wider scale (Daly, 1999). In Belgium married women used to stop working if their husbands earned enough, in the Netherlands women continue working if they can buy or obtain private childcare. Hence the relationship between family income, women's work and working hours is quite opposite in the two countries (Henkens et al., 1992).

The policies of Belgian governments concerning part-time work have been hesitant and inconsistent. Around 1980, part-time work was encouraged. The combination with part-time unemployment benefits made it a very popular option at the time (Casey, 1983). The program became too expensive and was in 1982 stopped because of its success. In recent years,

especially for older workers, the government has re-instated the possibility of combining part-time work with benefits. These options also exist in the case of part-time career breaks. The regional government of Flanders has introduced additional incentive schemes for part-time work and career breaks for the purpose of caring for young children and vocational training (Serroyen and Delcroix 1996: 47).

Part-time work is treated with ambivalence in labour law and social security, as well as in statistics. Until 1987 anyone working two hours per week or less was not counted and remained outside the social security system. When the 2-hours rule was abolished, employment rose by 55,000 extra jobs. Many workers became self-employed for tax and social security purposes (De Swert, 1999: 44). Mock self-employment is in Belgium what small part-time jobs of less than 12 weekly hours are in the Netherlands, except that since the 1990s the latter are covered by tax and social security. In Belgium, employment protection and minimum wage and vacation rights apply only to part-time jobs that exceed 1/3 of full-time jobs, with a minimum of 3 hours per day. In the Netherlands the opposite move took place, raising the status, rights and popularity of small part-time jobs, especially important in domestic services (Visser, 1999).

### *4.6 The efforts of a 'sur place'*

In professional cycling there is a game in which you have to work hard to stay in the same place and than leap to victory. This *sur place* appears a pertinent description of the Belgian case. There is no second country where governments have designed so many pacts, proposals, plans and schemes to coax unions into accepting wage restraint and employers into creating jobs, with so little success. There is also no second country where five Ministers of Labour, at the federal, regional and communal level, compete for attention and resources. The unanswered question is whether the new political situation will break the immobilism of Belgian politics —the Lib-Lab-Green coalition which gained power in 1999 has a clear mandate for change, after the string of scandals in recent years and disastrous electoral results for the Christian and Social Democrats, especially in Flanders. In conjunction with the 1998 central agreement, this may be the time for a new start. One promising proposal of the new government is to increase in 2000 'social Maribel' and to introduce a substantial reduction of non-wage labour costs, of about 32,000 BEF per year per employee for 'entry' wages. In total, the government wants to lower the 'tax on labour' with 50 billion BEF, to be financed with a tax reform announced for 2002 (but with a yet unknown content, except the lowering of VAT on labour intensive services from 21 to 6%).

Like the Netherlands, Belgium entered the 1970s with one of the lowest employment/population ratios in Europe. Thirty years later, unlike the Netherlands, the situation has deteriorated (Figure 3). Reducing labour supply is still accepted as an alternative to overt unemployment and government have gone along with subsidizing early retirement for lack of alternative. Unemployment has remained high, hides a large regional variation (with Flanders approaching full employment), and includes a large structural component, with the highest share of long-term and youth unemployment in Europe outside Italy and Spain. Like its Northern neighbour, Belgium went through a very difficult phase in the 1970s and sought to redress a rather desperate situation through a combination of wage restraint, fiscal consolidation and job sharing. While some of this worked and Belgium's external competitiveness was restored, the outcome in terms of employment was less favourable. Despite a large number of job sharing and job creation plans, employment growth remained sluggish. There was nothing compared to the growth in domestic services and part-time jobs experienced in later years in the Netherlands. In contrast to the Dutch economy in the 1990s, the Belgian economy, in spite of the recovery of its exposed sector, suffered from lacklustre consumer spending, The savings rate of households increased to an all-time high, and has remained high in 1995-1997. The OECD (1995: 7) speaks of a 'healthy financial position of households' and a show of 'low confidence'.

The various subsidy schemes have mainly affected the distribution of jobs rather than their overall number. Unions criticise that many of the schemes targeted at low-experience workers fail to re-qualify workers and instead trap them in dead-end jobs. Economists have raised the criticism that subsidies to firms, exposed to international competition, have lowered employer resistance to union wage demands and slowed down the rate of innovation. There are remarkably few hard facts or impartial studies on these issues. The only observations that can be made with certainty are: that there were many plans and schemes: that nearly all of them were contested; that many of these plans were designed to obtain co-operation from unions and employers, but very hard to monitor; that many were short-lived and depended upon complex implementation procedures; and finally, that the actual job creation rate was disappointing. The narrow employment basis of its economy, and the absence of a jointly held view on how that might be changed, suggests a continued vulnerability of this otherwise very wealthy country.

One may ask why there was not more policy change in response to stagnation and failure. Our main hypothesis is that organized actors in Belgium—inside and outside the government—failed to agree on the causes of the job crisis and its therapies, and that they continued to work at cross-purposes. Hence, the contrast in policies before and after 1982 found in the Netherlands is much less apparent in Belgium. Both countries suffered from lack of consensus and co-ordination in the 1970s and went through a deep crisis in the early 1980s. In addition to a massive rise in unemployment, Belgium also experienced a depletion of its national reserves, a crisis of international confidence and currency devaluation. Yet, Belgian trade unions did not accept that wage restraint and a recovery of profits were necessary conditions for economic recovery and job growth, as did the Dutch unions at the time. Was this a reflection of the continued strength of the Belgian? Did Dutch unions learn faster, in fact change paradigm, because they were so much weaker? The result was that in Belgian governments had to impose on trade unions and firms what in the Netherlands was negotiated between them. This restricted decentralisation and flexibility of wage bargaining in the Belgian case, made linkage with other policies, in particular work-sharing, more difficult and implementation-failure more likely. Moreover, its continued attempt to beg for support of its policy measures, made Belgian governments far more vulnerable to pressures of re-packaging wage policies with subsidies to firms and protective measures for the low-paid, and it compromised attempts at fiscal consolidation and welfare reform.

It is tempting to distribute some blame to the linguistic conflict and the cumbersome federalisation process, discussed in the introduction of this chapter. It overshadowed other pressing problems, like industrial decline, unemployment, public administration, justice or environmental decline (Swyngedouw and Martiniello, 1998). Michel Albert observed that the Belgians 'were amusing themselves with their linguistic squabbles' while the 'ship was sinking' (introduction in Hansenne 1985). The conflict was germane to government instability and produced a kind of 'crisis consociationalism', in which problems were combined until they were big, numerous or pressing enough to require a large coalition between parties each of which were allowed to deal with their own clients (Deschouwer 1998). The average tenure of Belgian postwar governments has been exceedingly short; in the ten crucial years between 1972 and 1982, when two major economic shocks needed a response, Belgium had no less than thirteen governments (compared to five in the Netherlands and only three in Austria). The weakening of the state was compounded by the partisan use of the state, with recruitment practices not based on merit but on party membership and the right combination of language and region (Deschouwer et al., 1996; Dewachter, 1987).

## 5. CONCLUSIONS

In the introduction we characterized Austria, Belgium and the Netherlands as 'birds of a feather', albeit of different colours. How come they did not 'flock together'? For the answer we must examine the external and internal conditions, the perception of problems, the policy choices and spill-over of unsolved problems and unhelpful choices.

The Austrian economy was hit less severely by the oil shocks, because it was and is less exposed to internationalization than the other two countries. Multinational firms were and still are lacking. The financial and stock markets were and are less developed, whereas Belgium hosts a number of very powerful financial holdings and the Netherlands traditionally had a highly developed stock market and a number of world-wide operating MNCs. Austria relied much longer and to a larger degree on all kinds of regulations, such as price, export and capital controls. Domestic oriented policies were maintained longer than abroad and the public sector played a greater role in buffering external shocks. With the passing of time, however, Austrian exceptionalism subsided. But its geopolitical location and particular history help explain why political actors shared the same fears and had the same problem perception: to avoid mass unemployment and hyperinflation, and to restore an export oriented, growing economy. The homogeneity of policy priorities is most prominently demonstrated in the amazing fact that income inequality was never a major topic in Austria and that wage moderation could much easier be maintained than in Belgium and the Netherlands.

The reasons for the poor performance of the Belgian and Dutch economy in the 1970s were not dissimilar. The high exposure to foreign trade was certainly a factor and meant that external shocks had a huge impact, but this was compounded by domestic factors, in particularly problematic wage setting, based on diverging objectives and insufficient co-ordination. The result was that corporate incomes had to bear the brunt of the adjustment in the terms of trade after the oil crises of 1973 (both countries) and 1979 (Belgium). In the Netherlands real wage growth stopped in 1979, whereas between 1978 and 1982 Belgium was alone 'among the seven small countries of Scandinavia, the Low Countries, Austria and Switzerland, in having a real wage increase' (Therborn, 1986: 150). Since small countries are price-takers in the international economy and the authorities maintained a fixed exchange rate policy, the export sector was unable to pass on the increased costs. The fixed exchange rate policy came at the price of very high real interest rates in the Belgium case. This worsened business conditions but did not attract sufficient foreign capital to offset the borrowing requirements of the public sector. The export sector could only stay competitive through above average productivity growth and had to accept lower profit margins, which in turn led to a decline in investments. The combination of real wage growth, rising non-wage labour costs and a strong external constraint explains the large drop in manufacturing employment. The deterioration of public finances alarmed the governments in both countries no later than in 1976, but attempts at reversing the trend were difficult in the light of unstable and internally divided coalitions and growing compulsory expenditure on account of rising unemployment and public dept servicing. In the Belgian case we may add expensive solutions to the linguistic conflict as well as the absence of any fundamental review of the institutional mechanisms of manpower deployment and wage determination in the public sector.

Looking back on 25 years of policy adjustment one is struck by the continuous importance of wage restraint for maintaining competitiveness and a hard currency for fighting imported inflation. Apparently there were no alternative policy options in economies exposed to international competition, not even in Austria. Debate over alternative tools has been rare in each of the three countries. The contrast between Austria and the other two countries shows that a hard currency choice is very harmful, even though unavoidable, if not combined with wage restraint. The Austrian example also shows that if organized in co-operation with the social partners, wage restraint allowed a possibility at fiscal expansion, and fighting unemployment, which the others did not have.

In negotiated political systems like Austrian, Belgium and the Netherlands, policy change is critically dependent upon the agreement of ruling coalition parties and support from the social partners. These systems may suffer from what Fritz Scharpf calls a 'negotiator's dilemma'. Negotiators must simultaneously search for effective policy responses, in terms of policy content, while resolving distributive conflict, i.e. find a 'fair' distribution of the social costs of adjustment between and among ruling coalition parties and the social partners (Scharpf, 1997). Perhaps because the problems were less pressing, but more likely because Austrian social partnership was less challenged from within, its governments and social partners had little difficulty of resolving the 'negotiator's dilemma' in the 1970s. All relevant actors, in both the political arena and the industrial arena, agreed over a Keynesian definition of the crisis, a definition which was contested by key actors in Belgian and Dutch economic policy making. Because of the conservative bias in Austrian society, there was no opposition to using foreign workers as a buffer by sending them home. This was not possible in the Netherlands and Belgium, and was by the time of the second oil crisis also ruled out in Austria. Austrian unions were rather unique in giving priority to full employment over income redistribution. This equalled an unfaltering policy choice for restraint. In the face of a much weaker Keynesian political consensus, Dutch and Belgian unions, in part as a result of union radicalization in the 1970s, were unprepared to forsake income redistribution for employment. The internal cohesion of the Austrian model was strikingly different from the situation in Belgium and the Netherlands, where the postwar consensus had in fact ended and was to be renegotiated within and between the different segments of society. Austria's legacy of a civil war between labour and capital in the 1930s and her position on the frontline between the communist East and the capitalist West bolstered the conviction that social conflict should be avoided at all costs. Moreover, Austrian social and economic policy making, more encompassing, smaller in number and more informal in style, appeared easier to co-ordinate than in the other two countries (Unger, 1997). There are very few checks and balances in the Austrian political system. Institutional arrangements such as a weak bipartite system, modest federalism, and grand coalitions allow governments to push through its issues, provided it has somehow engineered an agreement with the social partners. As is shown in numerous examples in the section on Austria, for instance the decision to privatise the steel sector in the mid-1980s, the 1988 tax reforms, the decision to join the European Union or the 1995 austerity package, agreements can be swiftly reached and promptly implemented. In comparison, the much more pluriform systems in the Netherlands and in particular in Belgium make for more cumbersome bargaining practices.

Lack of agreement in negotiated policy system is very costly. The more the Belgian and Dutch social partners proved unable to organise restraint, the more important the hard currency stance became. The resultant negative side of declining competitiveness led to soaring unemployment in the 1970s and early 1980s, which in turn exacerbated the cost explosion in social security, with the potential of a damaging cycle of increased non-wage costs, productivity hikes, unemployment and a fiscal crisis. Austria experienced neither of these two dire straits and was therefore in much better shape to stick to its incrementalist pattern of corporatist adjustment. Before 1987 Austria maintained virtually full employment, thanks to a joint consensus between political parties and the social partners over the merits of Austro-Keynesianism.

In the face of the acute unemployment crisis, a severe challenge to their power and pent-up frustrations over recurrent intervention, the Dutch unions finally conceded to the new realities of the world economy and returned to a strategy of wage moderation. Rather than continuing the prisoners' dilemma game, in which third party intervention had become unavoidable, they redefined their position in term of 'battle of the sexes', preferring a co-ordinated policy over distributive privilege. From 1982 on, Dutch unions have consistently placed jobs before income. This learning process on the part of the trade unions led to a revitalization of the social partnership in the Netherlands in the 1980s. Over time, wage restraint allowed for a rather smooth interplay between wage setting and fiscal policy, stimulating economic growth, while

keeping inflation down.

This painful learning experience did not occur in Belgium, where the social partners remained stuck in prisoners' dilemma and, moreover, suffered from internal fragmentation. Consequently, the government had to replace, and repay, the unions in the organization of wage restraint, accepting bargains with each over compensation through subsidies, make-work programs and measures for the low paid. Whereas the Austrian and Dutch social partners were successful in combining moderate wage increases with high level of flexibility at the micro level, the Belgium strategy of imposed wage restraint sacrificed micro-flexibility in the labour marker for the purpose of macro-adjustment. In addition, Belgian governments were faced with much larger implementation failures. Finally, they ran a much larger risk of being taken hostage and forced to renegotiate their preferred policies of austerity and reform of social security programs that repeatedly overran their targets. Of course, the options of Belgian governments were also limited by the fact that more money had to be spend on interests and repayment of debts and less was available for lowering taxes or propping up the spending power of workers and their families. Unlike the Netherlands, Belgium was unable to support wage moderation in the 1990s with tax rebates. Under conditions of permanent austerity the slightest of setbacks in economic growth had extremely dishevelling consequences for the country's public finances.

Austria's welfare state shows the highest continuity but also some signs of being out-of-date. But thus far, the political and institutional capacity for incremental reform and fast policy implementation has been high and overall performance is good, though not as good as it was. The flexibilization of the labour market progresses slowly. Pressures for changes towards a more liberal society, equal rights tend to come from abroad. The elections of 1999, returning the FPÖ as the second strongest party, demonstrate the persistence of Austrian conservatism and xenophobia, as well as some popular disenchantment with Austria's politics behind closed doors. Austria's problems as a welfare state seem much less urgent than its difficulties of transformation into a modern and open society. Belgium welfare state reforms are much more severe, because of larger and unsolved financial burdens, the federal conumdrum, less homogeneity of preferences, and, as yet, little learning experiences with successful, piecemeal reform. The Dutch welfare state certainly has experienced the greatest transformation and shown considerable capacity of reform and innovation. However, it stands now again at the crossroads, of how to spend its newly gained resources and re-assess the balance between public and private investment and responsibilities.

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