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**Why a Competitive Europe  
needs Competing Europeans**

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## Why a Competitive Europe needs Competing Europeans

### Europe's Malaise

There is a wide consensus today that the Constitutional Treaty, drafted by the European Convention under the guidance of VALÉRY GISCARD D'ESTAING and signed by the governments of all 25 Member States of the European Union (EU), did not fail in two referenda because the French and the Dutch are by majority against the European integration project. A more important reason is that the EU has failed to address the fears and worries of its citizens: Leaving aside the ten new Member States, unemployment in the EU-15 was stubbornly high at 7.8% in 2005, compared to 5.1% in the United States and 4.4% in Japan; per capita income was about 41% lower in the EU-15 than in the United States in 2005 by Purchasing Power Standards; and GDP growth has been about 1.1% higher in the US than in the EU-15 over the past 10 years and will be so again in 2006, further widening the income gap.<sup>1</sup> In the latest Eurobarometer (EC, 2005) "unemployment" and "the economic situation" were named as the two single most important concerns of Europe's citizens. To many it seems that 'old Europe' is becoming an obsolescent model in times of rapid globalization and demographic change in many European countries.

The need to adjust social and economic institutions is felt across Europe. There is, however, little agreement on the substance of these reforms. Concerns in France, Germany and other continental countries have been mounting over the growing influence of 'Anglo-Saxon capitalism'. France famously fears that 'Anglo-Saxon imperialism' could destroy its national and cultural values. A high-ranking German social democrat, Franz Müntefering, referred to "international capital" as "swarms of locusts that fall on companies, stripping them bare before moving on"<sup>2</sup>, stirring a lot of

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<sup>1</sup> Calculations according to Eurostat, online at <http://europa.eu.int/comm/eurostat/> (29/01/2006 18:15).

<sup>2</sup> Cited in The Economist, "Locusts, pocus", 5 May 2005, London, online at [http://www.economist.com/displaystory.cfm?story\\_id=3935994](http://www.economist.com/displaystory.cfm?story_id=3935994) (29/01/2006 18:47).

attention in the international media. In Britain, on the other hand, the poor economic performance in some of the big continental countries is blamed on rigid labour markets and overregulation. In his much-noted address to the European Parliament on 23 June 2005 the British Prime Minister, TONY BLAIR, said: “[S]ome have suggested I want to abandon Europe's social model. But tell me: what type of social model is it that has 20m unemployed in Europe, productivity rates falling behind those of the USA; that is allowing more science graduates to be produced by India than by Europe.”<sup>3</sup> The media already refer to this row over the future of the European social and economic model as the “war of ideologies”<sup>4</sup>.

This paper will argue that contrary to popular opinion the current dispute over socio-economic reforms in the European Union is not harmful, but helpful to keep Europe dynamic and competitive. It will sketch the way regional mentalities in Europe have shaped different European socio-economic models, explain why the harmonization of Europe into one ‘European model’ might not a good idea and show how the competition between these models serves Europe’s long term interests.

## Competing Mentalities, Competing Regions

The Europe Union is made up of 25 Member States. Although all 25 countries are part of the EU, its single market, its single currency (except Denmark, Sweden and the United Kingdom) and the Common Foreign and Security Policy, they are very different. The European Union’s citizens, sharing a common European citizenship that grants them (some) voting rights wherever they settle down inside the EU and free movement across the Union’s borders, have different

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<sup>3</sup> Tony Blair, Speech to the EU Parliament (23 June 2005), online at <http://www.number10.gov.uk/output/Page7714.asp> (29/01/2006 18:25).

<sup>4</sup> Die Zeit, “Klassenkampf in Europa”, 31 March 2005, Hamburg, online at [http://www.zeit.de/2005/14/Soziales\\_Europa](http://www.zeit.de/2005/14/Soziales_Europa) (02/02/2006 10:49).

languages and customs.<sup>5</sup> Mentalities vary widely across Europe and have led to different institutional systems.<sup>6</sup> This can, for example, be illustrated with the divergent concepts of what constitutes a case of corruption: In Sweden a promising political career can end because a junior minister uses a government credit card to buy groceries. By contrast, Italy's Prime Minister, SILVIO BERLUSCONI, was charged with criminal offences ranging from the falsification of balance sheets to flagrant bribery, from which he was never completely cleared. And yet, BERLUSCONI remains in office (Neuhann, 2005). Apart from criminal law systems, European countries differ in their degree of political centralisation (e.g. federalism in Germany and Spain versus centralism in France), the degree of codification of their constitutions (e.g. Germany versus the United Kingdom) etc.

Just as mentalities and political institutions vary widely across Europe, so do economic and social systems. There is no European social or economic model. Broadly speaking Europe can today be divided into five different socio-economic models: the Anglo-Saxon, the Nordic, the Continental, the Mediterranean and the Central European.<sup>7</sup> Nordic countries (including Denmark, Finland, Sweden and the Netherlands) feature high levels of welfare protection; benefits are extended universally independent of income. Anglo-Saxon countries (including Ireland and the United Kingdom) offer welfare benefits to those citizens in real need and make substantial use of measures to help the unemployed get jobs. The welfare system of continental countries (including Austria, Belgium, France, Germany and Luxembourg) is generally based on the insurance principle,

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<sup>5</sup> In fact, we find that many of the European states are themselves divided into sub regions, with their distinct history, dialect and tradition. In Germany you will find Bavarians to be quite different from Saxons, in Belgium the Flemish to be different from the Walloons and Tyroleans to be different from the Sardinians etc.

<sup>6</sup> It will not be attempted to explain here, how different social and economic institutions evolved across Europe. Cf. for example Jepperson (2002, page 65), who finds that "a variety of forces affected what forms of mobilization were institutionalized in the different European regions: the kinds of geomilitary, economic and religious forces charted in the macrohistorical literature."

<sup>7</sup> The distinction between different European social models goes back to Esping-Anderson's seminal book "The three worlds of welfare capitalism" (1990), in which he make a distinction between a "liberal", a "conservative" and "social democratic" system. Leibfried & Pierson (1995) and Sapir (2005) add the "Mediterranean" model. There are other systematisations of Europe's socio-economic models: Hall and Soskice (2001) distinguish only between "Liberal Market Economies" and "Coordinated Market Economies".

in which benefits are paid according to the amount of insurance premiums contributed. Mediterranean countries (including Greece, Italy, Portugal, Spain, Malta and Cyprus) rely heavily on employment protection and spend large sums of their welfare budget on pensions. Finally, Central European countries (including Estonia, Latvia, Lithuania, Poland, the Czech Republic, Slovakia, Slovenia and Hungary) are – contrary to popular claims – not ultra-liberal market economies. In fact, they retained a relatively high social security system.<sup>8</sup> (Barysch, 2005a)

The models have, at closer inspection, advantages and disadvantages: the Nordic model allows for very low income differentials, while maintaining steady growth; the Anglo-Saxon model has led to relatively high growth rates, among other things because of strong work incentive structures, but has comparatively high income disparities; while allowing for relatively few social cleavages, the social insurance systems in both the Continental and Mediterranean models have come under severe strain; and in Central Europe low taxes and few regulations have helped foster high growth rates. In his analysis of Europe's socio-economic models SAPIR (2005, page 6) concludes that "the case for reform is (...) strongest in the Continental and Mediterranean countries where the welfare state has become highly inefficient. By relying on strict employment protection laws it discourages adaptation to change and preserves the status quo. The system therefore reduces overall employment and raises unemployment."

## Suggested Cures

The relative economic success of some models puts the governments of less competitive regions under substantial pressure. Voters in Germany and France want to know why the United Kingdom's unemployment rate stands at 4.6% and Denmark's at 4.9%, while 9.5% of their fellow countrymen and -women are without a job. Instead of finding solutions to their socio-economic

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<sup>8</sup> It remains unclear what model the new Member States of the EU will follow, how they are going to bring relatively high welfare expenditures into agreement with their low-taxation policy, and whether a new socio-economic model that combines elements of these countries' communist past with liberal market economy concepts will emerge. (Cerami, 2005)

problems, however, these countries' governments call for harmonization and European regulation to offset the effects of competition between the regional models. Low corporate tax levels in Ireland, the United Kingdom and especially in many of the new Member States have led political leaders in Germany to denounce "unfair competition" and call for a harmonisation of taxes on EU level.<sup>9</sup> Instead of thinking about a genuine tax reform in Germany – where the tax code is said to be so complicated that there is no human alive that fully understands it – is looking for ways to evade the competition. Forcing the new Member States to adopt policies that clearly do not work in the old Member States will not help cure Europe's malaise.

Eager European federalists have proposed to introduce a single European social model. The proposal of the president of the European Commission, JOSÉ MANUEL BARROSO, to creating a 'Globalisation Adjustment Fund' is a first step towards a common European social budget. The fund "would provide financial help for training, relocation of workers, outplacement in cases where economic restructuring (and therefore job losses) occurs because of globalisation"<sup>10</sup>. Most economists agree that the European Union cannot solve the economic problems of its Member States. As the slow progress of the Lisbon Agenda suggests, declarations of intent on European level do not assure the implementation of desirable policies inside the Member States. The Union simply lacks the powers to regulate socio-economic policy on national level. It is moreover questionable whether the Union has the know-how to implement the suitable, customized solutions to address the specific problems of individual Member States. In sum, "Europe cannot and should not have a strategy for reforming national labour markets and social policies. It is up to each national government to devise its own strategy." (Sapir, 2005, page 7)

Neither European harmonization nor EU policies can be the solution to the structural problems of individual Member States. Each country should address the deficits of its own socio-economic model. Common European initiatives, such as the 'Globalisation Adjustment Fund', could in the

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<sup>9</sup> The Economist, "Tax wars – New versus old Europe", 22 July 2004, London, online at

[http://www.economist.com/displaystory.cfm?story\\_id=2951334](http://www.economist.com/displaystory.cfm?story_id=2951334) (30/01/2006 15:55).

<sup>10</sup> EURATIV, "New budget proposal increases pressure on Blair", 23 November 2005, Brussels, online at

<http://www.euractiv.com/Article?tcaturi=tcm:29-146150-16&type=News> (30/01/2006 16:17).

best case be helpful in flanking the adjustment programmes in the Member States by offering financial and technical support. Far more important to the European 'poor performers' will be the comparison with other Member States, both with those with a similar and those that follow a different socio-economic model. The right questions for the Member States to ask in this context are: What did the other Member States change in their system to create growth and employment? Could this adjustment work in our model? What were the costs and the benefits of the adjustment? How did other Member States manage to maintain support for their reform agenda? "Each country will have to find an answer suited to its own circumstances. But the EU, and its Lisbon reform programme, can help them to compete, compare and learn from each other." (Barysch, 2005b)

### From Competing Regions to a Competitive Europe

To sum up: Europeans are different by history, culture and mentality. They have developed distinct socioeconomic models, that behave very differently to the challenges that globalization and demographic change confront them with. Some of these models perform better than others. This is, however, no reason to harmonize these models into one. In the spirit of subsidiarity, the Member States of the European Union should maintain their own social and economic arrangements and find unique ways to solve the shortcomings of their regional systems. Maintaining different models within broad economic policy guidelines of the European Union, such as the Lisbon Agenda, will allow for competition, comparison and mutual learning between the Member States.

As globalization progresses, the world will face ever new social and economic challenges. If Europe starts treating its socio-economic diversity as an asset instead of a liability, system competition between Europe's different models might give Europe a stronger impetus for continuous change and adjustment. Embracing rather than rejecting this competitive dynamism might be what Europe needs to give it a competitive edge in a globalising world. Against this backdrop the ongoing dispute over "Anglo-Saxon" and "Continental" capitalism should not be treated as a sign of a break-up of the European Union, but be accepted as a part of an ongoing competition

between Europe's different socio-political models, its regions and its mentalities. This in its truest sense is what the European motto "United in Diversity" should stand for.

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