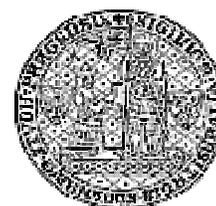


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European Social Models and Growth: Where are the Eastern European countries heading?

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European Social Models and Growth: Where are the Eastern European countries heading?

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August 2007

Abstract:

The authors find that as they seek to develop a social model both appropriate to their needs and consistent with EU standards, Eastern European countries must understand that a single European Social Model does not exist. Recently, some Eastern European unionists have begun to support their demands with reference to the European Social Model, which they only comprehend, however, in terms of its most inefficient Continental form. Eastern European countries must engage in a deeper public discussion of the pros and cons of various diverse social models, while taking into account the effects of different social models on the past and future competitiveness of the countries that have adopted them. Let those models compete to open opportunities based on forward-looking approach with full respect to the minimum harmonized standards (such as social safety net etc.) instead of fixing the past.

Keywords: European social model, competitiveness, welfare, public goods

JEL: H11, H4, I38.

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INTRODUCTION

The dynamic changes in social and economic systems throughout Europe, the structural changes in income and wealth distribution, regional distribution of economic activities, represent both core drivers and impacts of macro-, mezzo- and micro-structural changes that are hardly separable in causal chain. Their relevance goes, however, well beyond growth or economic world but spills over to political stability of the afflicted countries, of the EU and its position worldwide. What in 20th century has distinguished European countries from the rest of the world and internally and are those features sustainable?

A BRIEF HISTORY OF THE EUROPEAN SOCIAL (AND ECONOMIC) MODEL

As many authors have noted, in the first half of the last century, a perception of Europe as an inherently peaceful place striving towards a vision of social harmony would have seemed truly absurd (Wickham, 2002). At that time, much of the world was still dominated by European nations whose administrative power was ensured by their military dominance. Unsurprisingly, after the devastation caused by two world wars that erupted from conflicts within Europe, the desire for peace, tranquillity, freedom and prosperity emerged as one of the most powerful European ideals. At the end of World War II, millions of refugees were homeless, the European economy had collapsed, and 70% of the European industrial infrastructure was destroyed.

While some authors are trying to trace deeper historical roots¹, we join an often shared pragmatic view of the European Social Model as a product of the political settlement established at the end of the Second World War. Across all of Europe, a political consensus emerged among the forces that had opposed fascism, or at least those forces that no longer wanted to be identified with it, including both the political left (the trade unions, the social democrats, the communists) and the Christian Democrats (Wickham, 2002). Reforms in post-war Europe were concentrated on avoiding the social conflicts that characterized the time period during and between the wars, and therefore both polar extremes, totalitarian and pure capitalist theories of governance, were criticised and reprobated. Moreover, in order to prevent Europe from tensions possibly ending in further conflict, there was a movement towards the integration and interconnection of Europe through the creation of a type of European federation united by common interests, which was supported from many sides.

¹ Unfortunately the long-term development and implementation of contrasting models and sub-models of capitalism and socialism representing different approaches to notions such as equality and justice or value based thinking goes well beyond the scope of this article. „At least since the French revolution equality has served as one of the leading ideals of the body politic; in this respect, it is at present probably the most controversial of the great social ideals... In its prescriptive usage, ‘equality’ is a loaded and ‘highly contested’ concept.” – see Stanford Encyclopedia of Philosophy, 2007, Giddens 2006, etc.

Since the European Community arose from the European Economic Community, its early aims and goals were strictly economic (that included the introduction of “*welfare state*”), and purely social dimensions remained outside of its scope, leaving national member states utterly responsible for the social policies that determined the nature of their respective welfare states.

All EU member states were expected to maintain a balance between economic growth and social development. According to the Treaty of Rome of 1957, member states were required to support the balanced development of economic activities while simultaneously working towards a high rate of employment, the provision of social security, an increase in the standard of living and quality of life, economic and social cohesion, and solidarity between member states. However, for quite a long time the emphasis on the development of “*welfare state*” solving current issues outweighed the emphasis on certain social matters, despite the member states’ adoption of new documents promoting social issues.

A 1961 European Council document, entitled The European Social Charter, formed the foundation of the European Social Model. It established the main principles of the model: the provision of health insurance, social security, the protection of rights of the family and its status as a fundamental unit of society, improvement in working conditions and the right to education. Following the enlargement of the Community to include Ireland, the UK and Denmark, the Social Action Programme of 1974 instigated another wave of activity, particularly in instituting three directives outlawing gender discrimination in pay, employment and social insurance.

The term “social cohesion” is said to have been first used in the Single European Act (1987). In a socially cohesive society, people share a commitment to maintain social order and assume responsibility for the general social welfare in such a manner that their concern for society transcends immediate personal relationships. Cohesion is therefore somewhat the opposite of individualism.

For much of the 1980s, subsequent attempts by the Commission to develop a more active social policy were limited, not least by the return of the UK to an Anglo-Saxon social model and the UK government’s determination to veto anything that undermined the deregulation of the UK labour market. In the late 1980s, European integration was revitalized by the drive to create a single European market in 1992. As a reaction to this process, which exposed member states to competition on a European level, the Social Charter was adopted in 1989 “*to protect member states from the excesses of the market*” (Wickham, 2002). The discussion on “*the new welfare state*” has been triggered².

The term European Social Model is said to have emerged at the beginning of 1990s during the initial implementation of the Maastricht Treaty. The term was first used in a Green Paper issued in 1993 and later in a White Paper issued in 1994 on the future of social policy, which outlined a rather normative set of common values: personal freedom, social dialogue, equal opportunity and solidarity among all levels of society. The essential characteristics of this social model have not yet been clearly defined, and the various sources related to this topic only provide a general description of the model. In the words of Jepsen and Serrano Pascual (2005): “*One of the fastest growing European catchwords at the present time - the “European Social Model” (ESM) - is used to describe the European experience of simultaneously promoting sustainable economic growth and social cohesion. A clear definition of what constitutes its essence seems to be lacking in most documents on the subject, while a review of some of the most important of these documents reveals that, insofar as definitions are to be found, they do not necessarily converge.*”³ Diamantopoulou offers a different, more extreme interpretation of the

² *The new welfare state* should adequately solve the current problems not the issues of the past. See Esping-Andersen (2002)

³ In their article, Jepsen and Pascual aim to analyse and deconstruct the social model in order to identify its underlying ideological foundations and its various dimensions. They classify and discuss the ways in which the model is most frequently construed and propose a new approach to understanding this polysemy, arguing that the different dimensions of the concept

model (2003): “*The European social model: many claim that it is not really a model, it is not only social, and it is not particularly European.*”

As the European Parliament stated in its Report on a European Social Model intended to apply from July 2006: “*The European social model is first and foremost a question of values. Whatever European social system we examine we find the common values of equality, non discrimination and solidarity and redistribution as fundamentals.*”

After the signature of the Maastricht Treaty in 1992, European Union policy focused on the issue of single currency and the consolidation of the single market, leaving most of the decisions regarding the social and economic rights of EU citizens at the level of individual member states. Although EU documents did mention high level of employment and social protection as important aims, there were no associated criteria for their enforcement, contrary to the extensive treatment of the *acquis communautaire* with regards to economic issues (de la Porte and Deacon, 2002). Within the EU-25, health, transportation, pensions, education and other public services were almost entirely left to the decisions of national governments. Since the financing and regulation of the various social models are determined at the national level, regulation, taxation and redistribution levels vary widely across the Union. For details on differences in redistribution levels see Table 1. Canoy,Smith (2006) provide further comprehensive comparison of highly diversified national social protection expenditures both in its share of GDP and in different methods of financing and methods of delivery.

can be seen as rhetorical resources intended to legitimize the politically constructed and identity-built project of the EU institutions.

Table 1: Redistribution level in European countries

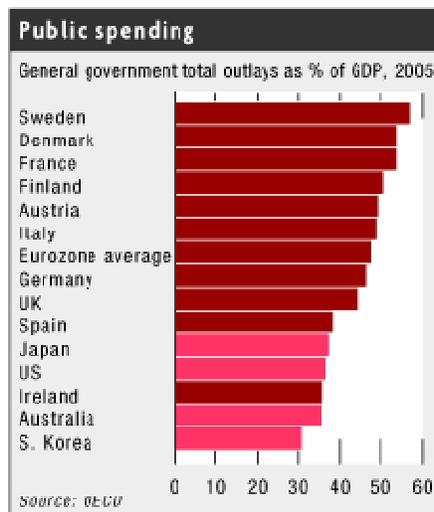
	Total taxes			Indirect taxes		Direct taxes		Top statutory personal income tax rate ¹ , %	Effective top statutory tax rate on corporate income ² , %
	<i>as % of GDP</i>			<i>as % of total tax burden</i>					
	1995	2001	2003	1995	2003	1995	2003	2004	2004
EU25	40.5	40.8	40.3	33.8	34.8	31.5	32.7	41.7	27.4
EU15	40.5	41.1	40.6	33.6	34.6	31.6	33.1	46.2	31.4
BE	45.1	46.2	45.7	29.5	30.1	37.9	38.3	50.0	34.0
CZ	36.2	34.5	36.2	33.9	31.4	26.5	27.1	32.0	28.0
DK	49.0	49.8	48.8	35.0	35.7	62.4	61.1	47.6	30.0
DE	40.8	40.7	40.3	30.1	30.7	27.5	26.7	45.0	38.3
EE	37.9	31.6	33.4	36.6	39.4	28.9	26.2	26.0	26.0
EL	32.6	37.0	36.2	44.1	39.8	23.8	24.8	40.0	35.0
ES	33.4	34.8	35.6	32.7	35.1	31.4	30.9	45.0	35.0
FR	43.7	44.7	43.8	37.1	35.5	20.7	26.8	49.6	35.4
IE	33.5	30.2	29.9	43.9	43.5	41.1	41.2	42.0	12.5
IT	41.2	42.5	42.9	30.9	34.5	37.4	35.6	45.0	37.3
CY	26.9	31.5	33.3	42.7	49.6	32.9	29.2	30.0	15.0
LV	33.6	29.0	28.9	40.7	39.7	23.2	29.3	25.0	15.0
LT	28.6	28.8	28.5	43.0	41.6	30.6	28.4	33.0	15.0
LU	42.3	40.7	41.3	31.9	33.8	41.6	38.6	38.0	30.4
HU	41.6	39.3	39.1	42.8	42.4	21.3	25.0	40.0	17.7
MT	26.9	31.1	33.6	46.0	42.6	31.4	37.1	35.0	35.0
NL	40.6	40.0	39.3	29.3	33.9	31.2	29.3	52.0	34.5
AT	41.3	44.7	43.0	35.8	35.1	28.3	31.1	50.0	34.0
PL	39.4	35.4	35.8	40.1	42.8	32.4	20.1	40.0	19.0
PT	33.6	35.7	37.0	43.5	43.0	26.6	25.3	40.0	27.5
SI	40.8	39.1	40.1	39.5	41.8	17.7	21.1	50.0	25.0
SK	40.5	32.0	30.6	38.6	37.6	28.6	23.6	38.0	19.0
FI	46.0	46.0	44.8	31.0	32.3	38.2	41.0	53.0	29.0
SE	49.5	51.8	50.8	32.8	34.5	40.8	37.4	56.0	28.0
UK	35.4	37.3	35.7	39.9	38.3	42.7	43.7	40.0	30.0

Source: Eurostat

1) The top statutory personal income tax rate reflects the tax rate for the highest income bracket without surcharges. The municipal income tax is included for Denmark, Finland, and Sweden.

2) The effective top statutory tax rate on corporate income reflects the non-targeted rate including surcharges and averages of local taxes. For Estonia the rate refers only to distributed profits, as from 2000 the tax rate on retained earnings is zero. The rate for Italy includes 'IRAP' (rate 4.25%), a local tax levied on a tax base broader than corporate income.

The most recent OECD data are confirming the situation of the old member states



CURRENT DISCUSSIONS OF THE EUROPEAN SOCIAL MODEL

The question thus remains as to what extent it is advisable to harmonize EU policies. In this respect, it is important to realize that the prevailing forms of the European social model only exist because Europeans accept the importance of the welfare state and value many of the public goods (provided originally by the state, now more by the private sector under regulation), both of which has been necessarily accompanied by the existence of a certain public sphere and a relatively high redistribution level.⁴ *The new welfare state* of Esping-Andersen(2002) should adequately address new risks and issues.

Scharpf (2002) argues that European integration has created a constitutional asymmetry between policies promoting market efficiencies and policies promoting social protection and equality. *“National welfare states are legally and economically constrained by European rules of economic integration, liberalization, and competition law, whereas efforts to adopt European social policies are politically impeded by the diversity of national welfare states, differing not only in levels of economic development and hence in their ability to pay for social transfers and services but, even more significantly, in their normative aspirations and institutional structures.”*

As a response to this fragmentation, the so-called “Open Method of Coordination” has emerged and is now being applied in the field of social policy. It leaves effective policy choices at the national level, but attempts to improve these policy choices through the promotion of common objectives and common indicators, as well as comparative evaluations of national policy performance. According to Scharpf, these efforts are useful, but cannot overcome constitutional asymmetry. *“Hence there is reason to search for solutions which must have the character of European law in order to establish constitutional parity with the rules of European economic integration, but which also must be sufficiently differentiated to accommodate the existing diversity of national welfare regimes.”* Scharpf presents two possible solutions: “Closer Cooperation” and a combination of differentiated “framework directives” through the Open Method of Coordination.

⁴ Wickham (2002) provides an example of some media being considered too important to be run purely for profit, since citizens have a right to good quality entertainment and impartial news which the market cannot be trusted to deliver. He believes that the state should also play a major role in providing basic education and health, since these involve notions of equity, which it would be difficult for a commercial company to apply. Esping-Andersen(2002) provides different view.

Although there is space for mutual cooperation and discussion regarding the effectiveness of different aspects of national policies, which could possibly lead to deeper discussions about the direction and guidance of social policy measures, different approaches towards social issues and different cultural patterns among member states make it in many cases impossible to implement the most effective practices of one member state into the policy framework of another. However, it is possible to enact significant changes that counter the natural direction of social development when those changes are promoted by a strong and charismatic personality. Margaret Thatcher, whose far-reaching liberalization policies of the 1980s revitalized the UK and reduced the unreasonable power of trade unions within the country, provides an appropriate example of this type of charismatic politician. The low frequency of industrial strikes has been maintained until the present and her reinvention of the Anglo-Saxon social model has since proved both sustainable and efficient. The culture she successfully redefined and reshaped has survived principal political changes with limited corrections.

Differences in tax rates and national regulations have generated criticism from number of EU new left regarding so-called „social dumping“. This concept suggests that lower tax rates or more favourable labour market restrictions in certain countries may create incentives strong enough to attract enterprises from countries with higher taxes and less liberal labour markets. Moreover, „social dumping“ is sometimes connected to the “race to the bottom”, in which countries compete with each other for the lowest tax rates and lowest degree of market regulation in order to entice new investors. While critics like Wickham (2002) are afraid of an eventual loss of social cohesion, we share the view that it is rather ideology than real threat as analysis of Kvist (2004) proved. We wish instead to raise other questions:

- i) Should lower taxes and reasonable deregulation not be connected with “race to the top” from a developmental point of view subject to the relevant social strategies on a national level?
- ii) In the face of current challenges, do excessive regulations and redistribution resulting from the prevailing social models adopted in different countries secure social cohesion within Europe? Are those regulations and redistributive measures compatible with a competitive and dynamic knowledge-based economy in a gradually globalizing world?

We should also at least mention the new Lisbon process as an attempt to focus on “growth and jobs”, together with the repercussions it evolved to bring the social agenda back in. The topic of flexicurity is also related to ILO 2005 meeting, but what is important is that in the meantime, it was adopted, by the EU and remained one of the flagships of the refurbished Lisbon process⁵.

In its Report on a European Social Model applicable from July 2006, the European Parliament summarizes the benefits derived from the application of the model as well as its future challenges. It states that although particular member countries have different social systems and have used different methods in instituting the values of the model, in general they aim to attain a balance based on active interdependence between economic growth and social solidarity, which is reflected in the model as a unity of values with a diversity of systems. According to the report, in the last 60 years, these values have allowed a growing EU to successfully become an area of greater economic prosperity and social justice.

⁵ Spidla, V. 2005, 2006.

EP Report declares the leading principles of the reform of the European Social Model (13th July 2006):

- 1. Stresses the necessity to preserve and enhance the values associated with the European social model – equality, solidarity, individual rights and responsibilities, non-discrimination and redistribution with access for all citizens to high-quality public services – in addition to the high social standards already achieved;*
- 2. Recalls strongly that only an EU based on economic and social cohesion that defends its common values can be strong enough to defend its interests;*
- 3. Is convinced that there is no alternative to urgently reforming economic and social systems where they fail to meet the criteria of efficiency and socially sustainable development and where they are inadequate to tackle the challenges of demographic change, globalisation and the IT revolution;*
- 4. Expresses its deep disappointment at the present growth rate in the EU which makes structural reform extremely difficult;*
- 5. Is aware of the widespread concerns among EU citizens regarding unemployment - especially unemployment among young people - exclusion, poverty, insecurity on the job market, and the potential failure of social security systems;...*

The issue of economic prosperity and especially its future projections is highly debatable and is discussed further in this paper. While keeping these issues in mind, the report acknowledges that there is a clear need to modernise and enhance the model in order to respond to demographic changes, meet the challenges of globalisation, and increase the adaptability of human resources to rapid technological evolution. It underlines the urgent need for a reform of the concept of the European Social Model in order for the model to play a productive role in the economy.

One of this paper's authors wishes to further comment on the discussion at the European Parliament in February 2006. He finds that the concluding EP compromise is vague, conflicting and confusing and overlooks global competitiveness due to the current absence of principal reform programs in key Eurozone countries. Such a situation creates room for the joint activity of smaller and medium size EU members (both new and old) in protecting their national policies in response to the growing competitiveness within the EU. This therefore necessitates a much deeper understanding of the nature of social models, which will be explored in the following chapter.

THE EUROPEAN SOCIAL “(SUB)MODELS” AND THEIR IMPACT ASSESSMENT

As mentioned above, the European Social Model has never been clearly defined⁶. As Salais (2005) remarks: “*European politics in social matters is too much complex, multifaceted and full of internal contradiction to be easily grasped with general concepts such as European social model.*” Usually, when politicians, economists or researchers talk about the European Social (and economic) Model, they have two distinctive features of this broad concept in mind: its dissimilarity to the “American model” and the emphasis on economic growth that is accompanied by development in the social sphere. Another important feature of the model is its predominantly normative character (Jepsen and Serrano Pascual, 2005); its underlying concepts are based on assumptions that were never established through the use of empirical evidence, which impedes serious analysis in further discussions.

While the name “European Social Model” as such has remained a rather loose term, a variety of other national models of social provision have been identified in a more specific manner. The most important national differences are apparent in the transfer system, tax-benefit system, welfare policies, and more generally in the proportion of state intervention and individually based insurance in the matters of pensions, health care, education, etc.

Studies of these models, or sub-models, have established several distinguishing criteria and have drawn comparisons from many different perspectives. Currently, there are four types of European social (sub)models commonly discussed: the Scandinavian (Nordic) Social Democratic model, the Continental Corporatist model, the Anglo-American (Atlantic) Liberal model, and the Mediterranean model. All of them, including Great Britain as the only European representative of the Anglo-American model, differ significantly from the American socio-economic model. While the rights to education, social security and health care and the universal availability of these services form an inherent part of all social systems in Europe, the American model emphasizes individual responsibility. In addition, employment rights, including unemployment and sick benefits, maternity leave, the regulation of working hours, etc., are much more generous in European countries than in the USA.

The differences in social policy between the two continents are evident in the **Anglo-American Liberal Model**, which exists in two forms. The first one, adopted by the USA, Australia, and New Zealand, is more radical. Benefits are focused almost exclusively on those most in need and are aimed at preventing poverty rather than ensuring a certain level of standard of living. Taxes are relatively low and labour markets are not heavily regulated. The continental version of the model is used in Great Britain. This version of the model is located somewhere in between the American version and other types of European models. For example, it employs more active labour market policies and greater support for families with children.

⁶ Social model or “European social model” is a frequently used but often not so clearly defined notion. Following simplifications made e.g. by V. Semerak we define a social model as a particular configuration of welfare related institutions and organization of economic life. Specifically it includes institutions related to:

- Organization of labour markets (minimum wages, rules governing hiring and firing of employees, degree of unionization and the power of unions)
- Social system and tax system (level of redistribution and resulting level of inequality)
- Pension system (the degree of reliance on a compulsory state organized PAYG system and the level of redistribution included in the system)
- The role and power of state in general (direct and indirect influence of state on economic activities, interventions into price mechanism, presence of structural or industrial policies)

The Scandinavian Model, used in Denmark, Finland and Sweden, can be characterized by an active employment policy, the significant role of the state, a high level of progressive taxation, and a high rate of female employment. In contrast to the Anglo-American model, the role of charity is negligible. The social system is almost entirely financed from tax revenues.

Within the Scandinavian model, specific features of the Danish (sub)model have been recently pointed out⁷. Its essential pillar is a long-term, sound and stable macro-economic policy oriented towards global competitiveness. In addition, it features a purely Danish invention, **flexicurity**, which is based on the belief that flexibility and security are not contradictory and can actually be mutually supportive (Madsen, 2006). Flexicurity consists of a flexible labour market with fewer restrictions on both hiring and firing, a high level of social security and an active labour market policy. In addition, the Danish (sub)model also has a centralised labour market with responsible social partners.

In 2005, the International Labor Organization supported the idea that flexibility, stability and security on the labour market need not be mutually exclusive and asserted that there were several Western European countries which have managed to balance all of these factors. For example, countries with more flexible labour markets such as Denmark, Finland or the Netherlands experience higher employment rates than France, Germany, Greece, Italy and Spain, where the labour markets are more rigid.

In November 2006, the European Commission has launched a broad public debate on the need to review the labour law systems. The discussion paper (Green Paper on Modernising labour law to meet the challenges of the 21st century) will ask Member States, employers and workers' representatives how labour law at EU and national level can help the job market become more flexible while improving security for workers. The consultation will remain open until March 2007. All earlier drafts were entitled "Adapting labour law to ensure flexibility and security for all". The change of title reflects criticism from employers' associations and member states such as Sweden and the UK, which said that the paper was pre-empting the results of the consultation for which it is the basis, rather than leaving policy options open. As any national specific model also flexicurity is not a problem-free.

From the beginning of the 1990s until 2005, the unemployment rate in Denmark fell from 12% to 5.5%. However, it is important to note that this positive development was not accompanied by a similarly successful increase in the employment rate. The number of people of working age that receive public transfer payments increased and the number of people in activation programmes like subsidized job training and job search assistance courses did not fall with the decline in unemployment figures

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- ⁷ Flexicurity was one of the main issues discussed at the European Regional Meeting of the International Labour Organization held in February 2005 in Budapest - Hungary.
 - Danish Prime Minister Anders Fogh Rasmussen gave a speech on the Danish model at the UMP conference on economic challenges held in September 2005 in Paris - France.
 - Per Kongshoj Madsen from the University of Aalborg presented his paper on flexicurity as a new perspective on labour markets and welfare states in Europe at the Informal meeting of EU Employment and Social Policy Ministers held in January 2006 in Villach, Austria.
 - In January 2006, French Prime Minister Dominique de Villepin proposed a new set of measures based on the „flexicurity“ model. One of reasons was to fight long-term unemployment indicating social exclusion.
 - Denmark's current low unemployment figures and its low social exclusion rates, coupled to output growth of over 3% have led the European Union to adopt flexicurity as its leitmotiv in its European Employment Strategy. In particular, Guideline No.21 of the *Integrated Guidelines for Growth and Employment* for the period 2005-2008 calls on Member States to "...promote flexibility combined with employment security and reduce labour market segmentation, having due regard to the role of the social partners".

(Andersen and Svarer, 2006). It increases segment of frictional unemployment that is relatively high in Denmark. But Danish employees change jobs more than 800,000 times a year, which means that about one third of the labour force starts a new job each year (Rasmussen, 2005). Finally, high employment in the public sector also contributes to low unemployment levels. While in Denmark 32.9% of employees work in the public sector, in Germany only 12.2% of employees do so (Gregor, 2006). Recent change in Swedish government illustrates well the growing dissatisfaction of population with current Swedish version of Scandinavian model that lead to the critical loss of Swedish performance and competitiveness in the last decades as demonstrated by Munhhammar J.,2006a,2006b. One should not idealize the Scandinavian model and deal with its deeper performance and cultural features carefully.

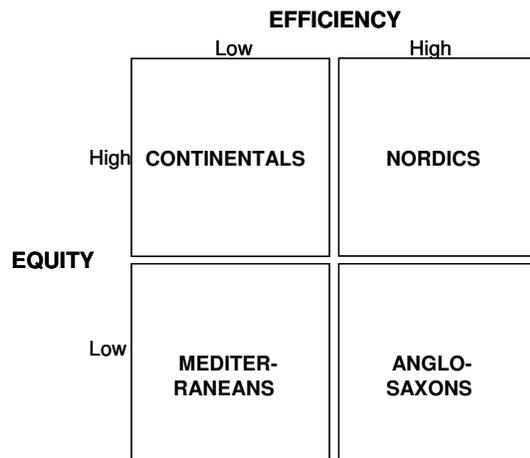
The Continental Corporatist Model is primarily used in Germany and France. This model places a strong emphasis on the role of labour law, which is elaborated to great detail. The working conditions of more than 90% of German employees are determined by collective bargaining. The employees also participate to quite a large extent in the decision making processes within enterprises. Another characteristic aspect of the model is the important role of the principle of subsidiarity, which entails an increased role of non-state institutions in the provision of public services. The role of women in society differs from that of the Scandinavian Model; female employment is very low and women tend to play a role within society that has been described by the term familism (e.g. Ostner, Reif and Turba, 2003).

The Mediterranean Model, primarily used in Italy, Greece, and Spain was until recently considered as a part of the group of Continental models with which it shares many similar characteristics. Social services are mainly financed through employees' payments. There is no comprehensive protection system, i.e. no guarantee of minimal income. Relevant decisions are made at the regional level, consequently contributing to large regional differences.

In the report of the Independent High-Level Study Group established through the initiative of the President of the European Commission (2005), Sapir defines the four types of social models listed above, and in addition argues that the notion of a single European Social Model is largely misleading since particular types of social models perform differently in terms of "efficiency" and "equity". A model is considered efficient if it provides sufficient incentives to work and equitable if it keeps the risk of poverty relatively low. Based on these two criteria, Sapir examines the typology of European (sub)models. He concludes that the Continental and Mediterranean models, which together account for two-thirds of the GDP of the entire EU-25 and 90% of the GDP of the 12-member Eurozone, are inefficient and unsustainable in light of the opportunities offered by globalization⁸. On the other hand, he considers both the Nordic and Anglo-Saxon Models efficient, but states that only the former manages to combine both equity and efficiency. However, a model that is not equitable may be sustainable, whereas an inefficient model is not. Therefore, it is more essential to move towards efficiency than towards convergence.

⁸ See also Aiginger,Guger (2006)

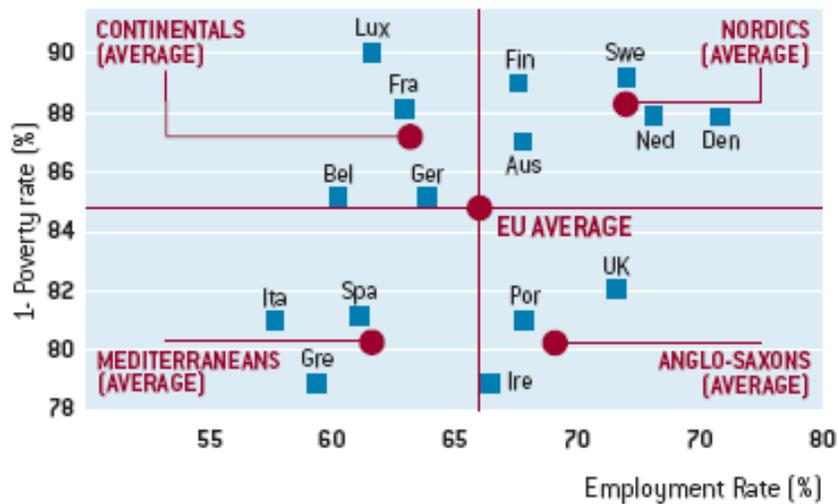
Chart 1: Sapir's typology



Source: Sapir (2005)

Differences in employment rate and the probability of escaping poverty (described as poverty rate), according to which particular (sub)models can be distinguished, are provided also by Sapir and depicted in the Chart 2.

Chart 2: Employment rates and the probability of escaping poverty



Source: Sapir (2005)

Table 2 illustrates the differences in additional indicators that quantify the role of the state, inequality and the economic performance of countries with respect to the above-mentioned (sub)models. Indicators for the USA and the Czech Republic are also included. While the indicators' values vary greatly across particular European states, none of them reach the indicator values of the USA, where a significantly lower level of redistribution and higher inequality go hand in hand with better economic performance.

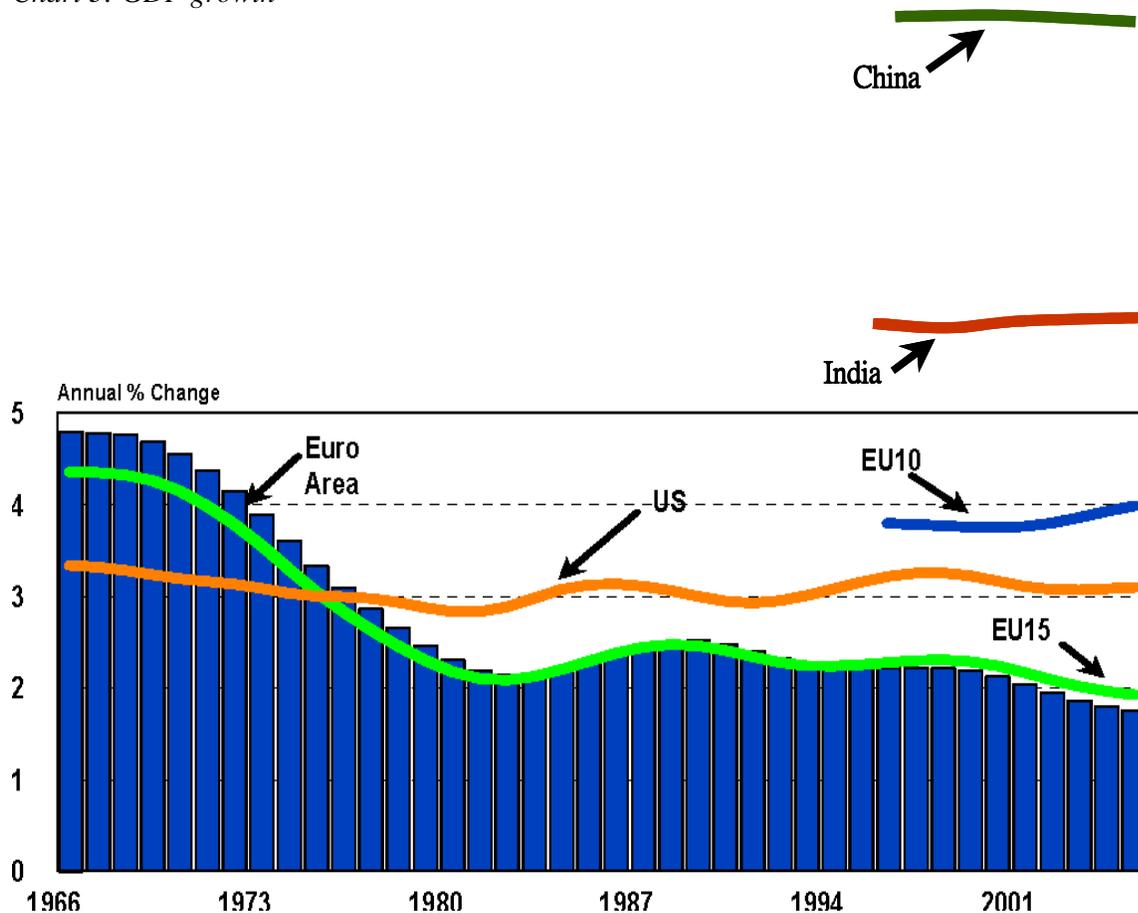
Table 2: Selected economic and social indicators

	Governmental expenses (2003; % of GDP)	Share of poorest quintile in income (The most recent year available; 2002)	Share of public health expenditures on total health expenditures (2002; % of GDP)	GDP growth (1990-2003; average annual % growth)	Gini index (2000, 1999 UK, 1996 Czech R. %)
Sweden	37.2	9.1	84.8	2.3	25.0
Germany	32.8	8.5	78.9	1.5	28.3
Italy	39.6	6.5	75.3	1.6	36.0
UK	39.7	6.1	83.1	2.7	36.0
Czech Republic	38.2	10.3	91.4	1.4	25.4
USA	21.0	5.4	45.2	3.3	40.8

Sources: World Bank – 2005 World Development Indicators; United Nations – Human Development Report 2005

Regardless of the type of social model to which they subscribe, the European countries have a higher level of redistribution, more favourable inequality indicators, and greater availability of public health and other social services than the USA; however, the USA performs better economically. Chart 3 depicts a more long-term comparison of the economic development of European countries with that of the USA. In addition, the chart includes the much higher growth rate of Chinese and Indian economies for the purposes of comparison.

Chart 3: GDP growth



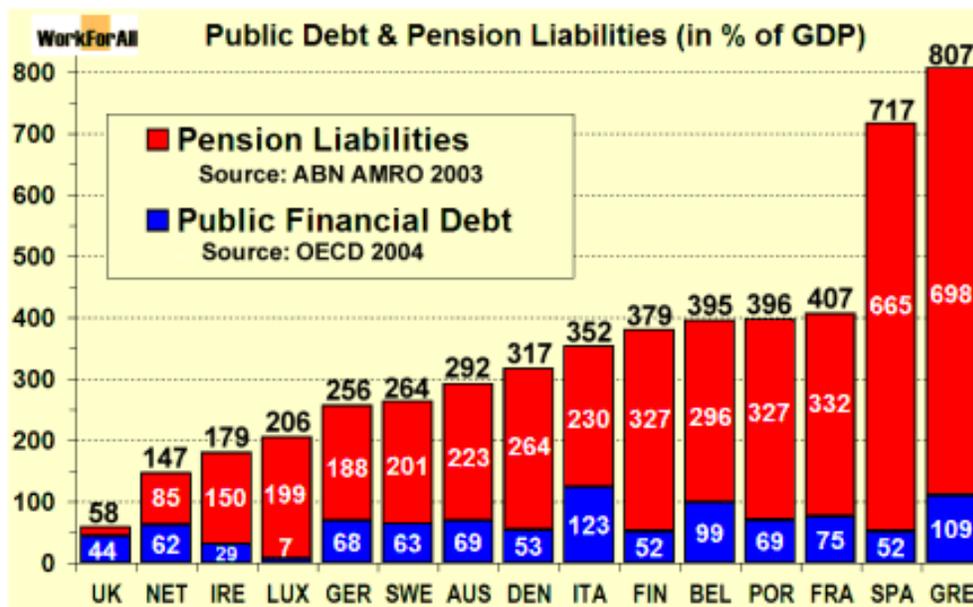
Source: EU Growth Trends at the Economy-Wide and Industry Levels, European Commission, April 2006; World Bank, 2006 World Development Indicators

Not only is the recent and current development of European economic growth worse in comparison to that of the USA, but the outlook for future development and current dynamic aspects of the economy are also of crucial importance. We demonstrate future threats in Chart 4 and Chart 5.

We concur with De Vlieghe and Vreyman's (2006) assessment that *“the reality of Europe's ailing economy contrasts sharply with its economic potential and with the massive resources employed to cure its ailing growth. The whole arsenal of Keynesian remedies has now been tried and has failed one by one. Massive deficit spending throughout the eighties and nineties has left Europe with a public debt unequalled in history. The size of Europe's monumental public debt is only surpassed by the hidden liabilities accumulated in Europe's shortsighted pay-as-you-go public pension schemes. Unfunded pension liabilities now average some 285% of GDP more than 4 times the officially published public debt figures. Total public liabilities now exceed assets in most EU countries, and are causing runaway debt service. Unfortunately, this will just kill growth completely. Europe's present social model is unsustainable because it is based on robbery of future generations...the workforce is de-motivated, and that Europe's personnel and managers are increasingly rebelling against the persistent confiscation of over 50% of the fruit of their labour.”*

Chyba!

Chart 4: Public debt and state pension liabilities (in % of GDP)



Source : De Vlieghe Vreyman's (2006) based upon ABN Amro(2003) and Hedbávný, Schneider, Zápál (2004)

In Chart 4 the state pension liabilities were calculated using the net present value of the implicit debt of publicly-run state pension schemes to predict the debt accumulated by 2050, based on unchanged policies. We agree with Hedbávný, Schneider and Zápál (2004), who point out that widely used European measures and frameworks are inadequate: *“neither Stability and Growth Pact rules nor their pre-EMU counterpart, the Maastricht criteria, take into account unfunded liabilities of governmental*

*programs. They tackle just explicit deficits and debts. Subsequently, politicians replace budgetary outlays with promises, the costs of which will be born by future taxpayers”*⁹.

Here one should temper the above statements with the admission that the off-budget liabilities accumulated in Europe’s short-sighted pay-as-you-go public pension schemes are a function of the current country specific level of key parameters (such as retirement age, contribution rate, defined benefits, etc.) reflecting current political status, as implied in the term “unchanged policies”. Due to their sensitivity to parameter change (e.g. rise in the statutory retirement age), a guaranteed reduction of those hidden liabilities is critically dependent on political will and therefore not easily predicted. Lowering the current social comfort due to the internalization of future costs is politically painful.

As reflected in Joint report EC on social protection and Inclusion (2007) after huge effort „pension schemes generally manage to ensure adequate retirement income in most Member States at present, in particular statutory schemes and those private schemes that are spread widely in terms of coverage. **Future adequacy** and, in particular, future levels of pensions in relation to earnings (income replacement levels) will depend notably on the pace of accrual of pension entitlements (which is linked to developments in the labour market), the maturation of pension schemes, the indexation of benefits and **the effect of reforms introduced.**“(p.32 report Annex) The globalization and aging are, however, only multiplying core problems¹⁰ : “***A job is the best safeguard against poverty and social exclusion...(with limited problem of in-work poverty)***“.

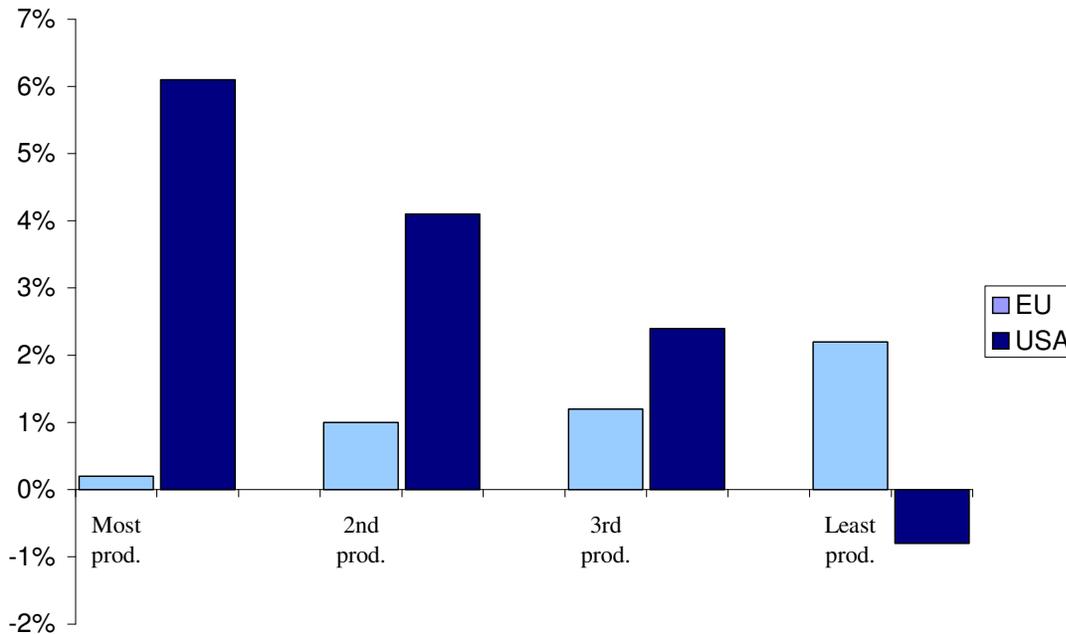
THE EUROPEAN SOCIAL “(SUB)MODELS” AND STRUCTURAL CHANGES

As depicted in Chart 5, deep structural changes on the labour market are obviously much more growth enhancing in the USA than in Europe. In historical terms, during the 1970s, unemployment in the USA increased, but even more so in Western European countries. In the 1980s and 1990s, American unemployment went down while simultaneously wage inequality increased significantly. In contrast, European unemployment fluctuated without any important changes and wage inequality changed only slightly. Throughout the 1980s and until the mid-1990s, Europe experienced higher growth in labour productivity than the USA. However, starting in late 1990s, productivity in the USA began to accelerate and rapidly overtook Europe, which might have important consequences for the future development of European economies. These disparities can broadly be explained by technological progress and the diffusion of innovation, in which Europe has been lagging behind (Trichet, 2006). What then about the labour market?

⁹ Hedbávný, Schneider and Zápál (2004) suggest the use of a mechanism they call the Sustainability Council. „*This would allow to prepare for a fast increase in expenditures as baby boomers head for their retirement and will draw public pensions and use public health care programs enthusiastically.*“ See EC age related expenditure projections in Canoy,Smith (2006).

¹⁰ Canoy,Smith (2006) properly declare: „*The problems that social and labour market institutions are facing today are often attributed to globalization and aging. This article argues that globalization merely exposes inherent weaknesses in social institutions while aging aggravates them.*“ See also results of more theoretical approach of Boeri at al.(1999).

Chart 5: Growth of Employment by Productivity Quartiles is a Long-Term Signal



Source: Gretschmann (2006)

In many cases European labour markets need more flexible rules, which would encourage competitive behaviour and the development of forward-looking structural changes. Chart 5 demonstrates that European “comfort-oriented” economic practices protect the least productive sectors, while US (and Chinese) market driven tendencies do exactly the opposite. These diverging labour allocations not only signal ex post trends but also ex ante, longer-term structural changes that could potentially cause a further decline in competitiveness multiplied by diverging hours worked¹¹.

To remain competitive with quickly economically growing countries such as India and China, Europe should use to its advantage its solid human capital resources as well as give more extensive support to education, research and innovation in order to increase productivity. According to OECD data from June 2006, European Union countries spend on average two thirds of the proportion of their GDP that the USA spends on research and development, while Japan spends an even larger amount (see Chart 6). Here one must be careful not to confuse quantity and quality of education and should avoid a deep structural mismatch of longer-term demand and the supply of an educated population¹². Such a mismatch often results from blind financial intervention by the government and regulation inspired by “good intentions.” The authors believe that a more adequate form of university funding, like the English system of higher education funding based on income contingent loans, can mitigate such a problem.

It is worth repeating that these suggested measures are not limited to the strict necessity of investing in research and development. As Švejnar (2004) argues, unlike the USA, which has eliminated most of its inefficiencies and must now look to inventions and innovation for growth, Europe still has considerable unexploited possibilities (X-inefficiencies) that can propel it rapidly forward such as inappropriate labour market institutions. We agree and posit that greater flexibility in European labour markets, as instituted within the framework of the social models mentioned above, would support competitive behaviour and forward-looking structural changes and reward it accordingly. Given the legislative

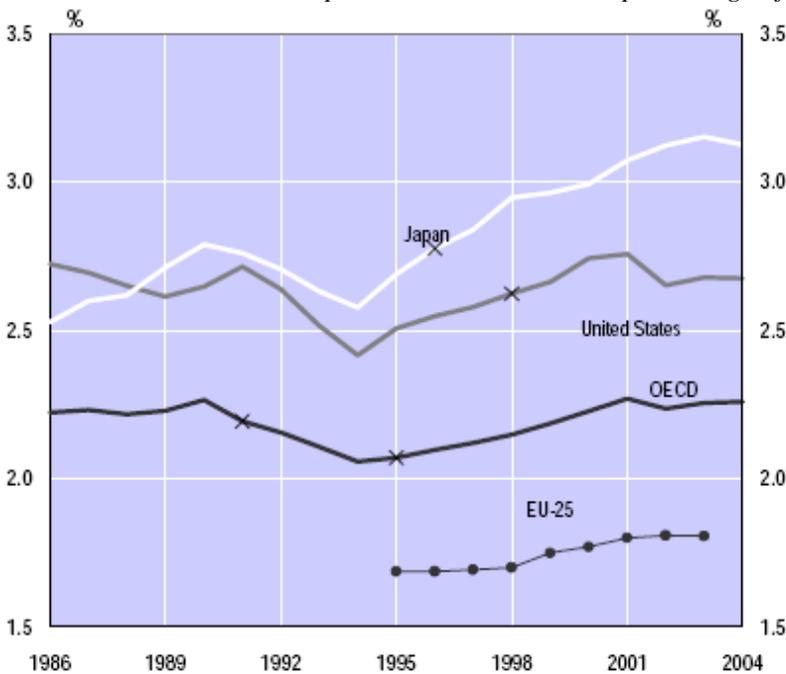
¹¹ See policy background discussion of European preference for leisure in Alesina, Glaesar, Sacerdote (2005).

¹² Number of those disequilibria can be identified e.g. within Italian higher education system.

initiatives planned for the end of 2005 and the beginning of 2006 (interim report on the transitional measures, final report of the “skills and mobility” action plan, proposal for a directive on the portability of pension rights, launch of Europass and of the new European portal on workers’ mobility), the ECommission has proposed making 2006 the European Year of Workers’ Mobility but the impact of that fact has been rather limited and symbolical.

Part of the reason for this can be attributed to the worldwide development of service sector that has dominated GDP formation during last decades. The failure to open the services sector to the European single market, which was ostensibly one of the European integration building pillars, contributes to the further perpetuation of inefficiencies in the most dynamic sector of the economy. A comparable dynamic service sector is highly productive in the US, but less so in Europe. Unfortunately, the reluctance of politicians to confront the politically painful impacts of both service market liberalization and the implementation of legislation promoting increased labour market mobility in Europe ¹³ overshadows the potential gains resulting from the elimination of inefficiencies within the services sector. The socially and politically painful reallocation of employment from the least to the more productive sectors is absent. It is no surprise then that there is a lack of demand for research and development in Europe; it can hardly be rooted in the well-protected, least productive sectors. And the state interventions in the field of human capital development and R&D can often be counterproductive in such unfriendly market conditions.

Chart 6: Gross Domestic Expenditures on R&D as a percentage of GDP



Source: OECD, Main Science and Technology Indicators, June 2006

Building upon earlier ESM definition, it is easy to understand that structural changes are very closely linked to the configuration and stability of social models, and that this relationship is bidirectional:

¹³ See the case of French discussion over Polish plumbers at the last part of this paper.

1. Configuration of social model has clear implication for the efficiency, speed, and stability of structural change. Speed of changes in an economy with excessive level of redistribution and high unemployment benefits is likely to suffer from employees' lower motivation to improve their qualification or look for work in other sectors or regions. On the other hand, fast structural changes in an economy without reasonable welfare system may lead to public discontent and subsequent reversal of reforms.
2. The speed of structural change matters for the stability of social models. Drastic shocks that cause sudden increases in unemployment may lead to serious problems of existing social system.

Then we can understand the opinion of EC 2006 : „There is broad consistency between the National Reform Programmes (NRPs) and Member State commitments at EU level in terms of social policies through the open method of coordination for social inclusion, pensions and health. The NRPs recognise that the exclusion of people and groups from participation in society and the labour market is a waste of resources which should be addressed for economic and social justice reasons. Pension reforms aimed at strengthening sustainability are improving the incentives for working longer. The adequacy of pensions now depends on opening labour markets for older people and fighting segmentation. Some NRPs (especially in new Member States) stress the importance of health issues as a precondition for raising the quantity and quality of labour : *Ensure inclusive labour markets, enhance work attractiveness, and make work pay for job-seekers, including disadvantaged people, and the inactive*“.

The protection of numerous inefficient domestic service jobs is short-sighted and blocks spontaneous structural changes supported both by flexible labor markets and by number of other critical conditions developed by Aghion et al (2006) such as more international competition and entry on the product markets, more developed internationalized financial sectors and markets besides larger and more efficient investment in higher education.

EUROPEAN SOCIAL MODELS AND THE NEW EU MEMBER STATES: EACH STATE SHOULD LEARN FROM THE BEST PRACTICES AND AVOID THE WORST PRACTICES

Although the social role of the state differs significantly between Western European countries, as demonstrated in the above-mentioned social (sub)models, the contrast is even more significant in the comparison between Eastern and Western Europe. In words of Bohle and Greskovitz (2004), the *“European Social Model ...has not travelled to the East” yet.*

In 2001, social expenditures in all the new member states remained below the EU-15 average. The Baltic countries (together with Ireland) followed by the Czech Republic, Hungary and Slovakia had the lowest social expenditures in the EU (see Table 3).

Table 3: Social expenditure in the new member states and EU-15 (2001)

	Total social expenditure (% of GDP)	Structure of social expenditure (% of total)						
		old age and survivor pensions	sickness	family benefits	disability pension	unemployment	social exclusion	housing
EE	14.3	42.6	31.0	14.6	7.8	1.3	2.2	0.6
LV	14.3	56.4	19.1	10.1	9.6	3.6	0.6	0.7
LT	15.2	47.5	30.0	8.3	8.8	1.9	2.3	1.2
SK	19.1	38.2	35.0	8.2	8.1	3.6	6.5	0.4
CZ	19.2	42.5	34.6	8.2	8.5	3.1	2.7	0.6
HU	19.8	42.4	27.5	12.9	10.3	3.4	1.0	2.5
PL	22.1	55.3	19.2	7.8	13.3	4.3	0.2	0.0
SI	25.5	45.5	31.4	8.9	8.7	3.7	1.8	0.0
Average	18.7	46.3	28.5	9.9	9.4	3.1	2.2	0.8
EU-15	27.6	46.1	28.0	8.0	8.2	6.3	1.5	2.1

Source: Keune (2006)

In terms of economic performance, although the GDP growth of Central and Eastern European countries is obviously higher than the growth rates in Western Europe, these countries' development growth cannot be compared to that of the ex-Soviet countries. In their paper, Aslund and Jenish (2006) find that since 2000 the Commonwealth of Independent States countries have had more than 4 percentage points higher annual growth than the Central European countries. Based on a regression analysis, they claim that the reduction in public expenditures has been the most effective stimulus of economic growth. Moreover, they find that the further from the European Union the country is located, the higher its economic growth. This is partly due to the catching-up process – given reasonable institutional conditions, a lower GDP base and underutilized growth potential open space for more rapid growth – but certain part of growth might be also due to the liberalization framework adopted by those countries.

When the people in European countries were asked how satisfied they were with their life, there was a significant difference between the responses in the EU-15 countries and the new member states. While the satisfaction index of the EU-15 reached 7.3 out of 10, citizens of the new member states rated their well-being at only 6.1 (European Foundation for the Improvement of Living and Working Conditions; 2003). Not surprisingly, the unemployment level emerged in the research as one of the most important factors affecting the level of satisfaction. Moreover, workers in the Eastern countries also work more hours per week and work safety is often lower, as well as union density.

On the other hand, it is necessary to add that social benefits applied in the labour market very often undermine and reduce the incentives of the unemployed to find a new job. The more targeted the benefits are to the poorest groups, the more they interfere with work incentives (Schneider and Jelínek, 2001, Tvrdon, 2006). Also, other policy measures such as increasing minimum wage and subsistence level affect employment development in a negative way. Therefore, generous social benefits can contribute to higher unemployment and prevent needed structural changes and limit mobility. How those Central Eastern European countries fit into simplified models or do they represent a specific submodel?

European Commission report *Employment in Europe 2006* in its 5th chapter clustered 18 EU Member States including new member states into groups based on flexicurity systems/models by

PCA-CLA methodology¹⁴. This EC report identified five country groups including submodel in the Eastern Europe (plus Italy) :

1. the Anglo-Saxon system (the UK and Ireland were included there),
2. the Nordic system (including Denmark, the Netherlands, Sweden and Finland)
3. the Continental system, (Germany, Belgium, Austria and France)
4. the Mediterranean system, (Spain, Portugal and Greece)
5. the Eastern European (plus Italy) system including Poland, Hungary, the Czech Republic and Slovakia and Italy

In their study for EALE 2007 conference Eamets, Phillips et al. (2007) tried to develop this PCA-CLA approach further for more EU member states that resulted in six different country groups. Then they tried to characterize each of these country groups by certain weak and strong features from the labour market performance point of view (they calculated average value of variables used in principal component analysis by different country groups, see Table 4):

The results of Eamets et al (2007) with respect to the flexicurity features suggest certain split of the Eastern European EU member countries into two groups – more dynamic Baltic and somewhat cumbersome Visegrad countries¹⁵. Anyway in spite of differences we can monitor rather slow (or sometimes even neglectable) legal incorporation of the Continental social model (prevailing in Eurozone) in rapidly growing and increasingly competitive Eastern European new EU member states resulting from, among other reasons, subjective perceptions and inclinations towards a more individualistic approach following the collapse of the socialist era. According to Večerník (1993), as people sought to escape socialist paternalism and enforced social entitlements such as unified corporate housing or corporate holidays, the general perception of the word “social” became increasingly negative. However, attitudes change in the course of time, and the initial optimism towards capitalism and individualism was slowly dampened. Although working and living conditions have not deteriorated considerably for majority of the population, an increasing number of citizens are again becoming attracted by the state protection of jobs and rents and price control. A large number of people have also been attracted by the “social market” model, and the percentage of people supporting a return to “real socialism” more than doubled in the period between the 1992 and 1998 elections (Večerník, 2004).

¹⁴ Member States were classified in a particular group/system according to an overall measure of “distance” (between countries) reflecting the scores obtained for the principal dimensions (identified in the principal component - PCA analysis) that characterise flexicurity systems (e.g. security, flexibility, etc.) and clustered then through K-cluster or hierarchical cluster analysis based upon calculated scores. PCA itself is a multivariate analysis technique that aims to evaluate how different variables are associated with each other. See the report.

¹⁵ It is not anything surprising. I agree with V.Semerak comments : „to ensure economic and political stability, the social model must be consistent with the level of economic development, the intensity of structural changes, and social preferences of the population (at least the preferences of the median voter). On the one hand, the Visegrad countries are located in the same geographical space as Austria and Germany and share with these two countries also large part of their history. This could suggest that at least as far as preferences of voters are concerned, the Visegrad countries may be relatively close to the “Continental model”. This being true, there are two important aspects that would cast some doubts on these predictions. Firstly, the experience of the last 50 years (centrally planned economy + subsequent substantial transition) substantially changed the intellectual climate in the Visegrad countries. Secondly, even if the voters’ preferences were the same, the countries cannot afford so developed welfare states as the richer EU members.”

Table 4. Average value of variables used in PCA sorted by different country groups calculated by Eamets,Phillips et al.(2007)

Variables	AT, BE, LU, FR, DE	NL, UK	DK, SE, FI	CY, IR, EE, LT, LV	EL, IT, MT, ES, PT	CZ, HU, PL, SK, SL
Total expenditure on social protection (% of GDP)	28,4	27,4	29,8	14,7	22,9	21,2
Total expenditure on social protection per head	7769,0	7347,3	8651,7	2165,9	3957,6	2453,0
Tenure	37,6	30,0	37,3	24,8	29,8	34,4
Unemployment insurance	37,2	23,0	39,0	18,0	16,6	13,2
Easiness of finding new job	16,2	29,0	35,0	27,2	9,8	12,8
Mobility	7,8	18,0	21,0	6,8	6,2	4,4
Training	25,2	38,0	43,3	23,2	15,0	21,4
Life-long learning	8,2	19,3	28,6	7,3	4,2	7,3
Part-time workers	18,2	35,4	19,1	10,8	8,4	5,7
Long-term unemployment rate	37,7	24,6	21,2	38,5	44,7	52,8
Unemployment rate of the young	15,4	9,3	14,8	16,3	21,3	24,9
Employment rate of 55-64 years old	33,1	49,9	59,5	48,1	39,3	29,2
Gini coefficient	27,6	30,5	24,7	31,4	33,4	27,2
Poverty (50%)	7,6	8,5	5,7	10,2	11,8	8,6
Trust	29,6	45,0	63,0	24,2	24,8	20,6
Early school leavers	12,2	15,5	9,2	14,3	31,8	6,7

Note: yellow/grey area indicates best performance in terms of flexicurity; numbers in bold indicate worst performance.

Their results are similar and confirmed by „common sense“:

1. UK and Netherlands represent the Anglo-Saxon model with quite liberal and flexible labour markets, low unemployment, high mobility and quite high general trust.
2. The cluster of Denmark, Sweden, Finland has its common „flexicurity“ features (described as a Nordic Model) and all Nordic countries have top scores in most of the indicators presented in table of Eamets,Phillips et al.(2007) and are used as a benchmark then.
3. The continental economic and social model is reflected by a cluster of the old EU member states – Austria, Belgium, France, Germany and Luxembourg. The preferred high social protection is complemented by comparatively the worst tenure suggesting the rigid labour market with one of the lowest mobility.
4. The cluster of Greece, Italy, Portugal, Malta, Spain (described as South European or Mediterranean Model) is characterised with poor labour market adaptability and low income protection. Surprisingly low are training and education indicators. Unemployment is at relatively high and employment relatively low level.
5. In the fifth rather heterogeneous cluster Eamets et al (2007) grouped fast growing, low-income economies in Baltics (Lithuania, Estonia, Latvia), Cyprus and high-income Ireland. Labour market flexibility indicators in this group are relatively high, but social protection is lowest in EU and also income protection is at relatively low level. Eamets et al (2007) are afraid of some indicators being probably overestimated and some underestimated.
6. The last group represents new member states from Central Europe – Slovakia, Czech Republic, Hungary, Slovenia and Poland, labelled some times as Visegrad countries (except Slovenia). Eamets et al (2007) are of the opinion that from the point of view of flexicurity together with Mediterranean countries this group is not doing very well. Labour market mobility is relatively low and long-term unemployment rate is high, elderly employment rate is low – all these are indicating that adaptability of labour market is relatively low.

EUROPEAN SOCIAL MODELS AND THE NEW EU MEMBER STATES DOMESTIC AND FOREIGN POLICIES

Policy discussion of different European Social (and Economic) Models further pointed out the issue of the impact of Eastern European EU enlargement on the growth of the old EU member states. We share the opinion of D.Daianu (2006) that “eastern enlargement is not solely to blame for the pain currently being experienced by EU member states, though it may have accentuated these problems...” having their both external and internal roots. We agree to include among external factors both “the race for competitiveness in today’s world and the rise of economies in Asia...and among internal factors the inner dynamics of European societies (demographics, the crisis of the welfare state)” but we should consider deeper relevant policy options for Eastern European social (and economic) submodels in future. And then we should raise an issue - are any Eastern European submodels stable and sustainable ?

Originally cumbersome legislative application of inefficient forms of the European social model disregarding new member states’ domestic conditions has been recently significantly refined under the umbrella of the harmonization of the *acquis communautaire*“ by several governments due to a political cycle (and new institutional labour market rigidities were born). It is perhaps nonsensical to discuss harmonization when the most of the social and economic rights of EU citizens still remain at the level of their individual member state. Nevertheless recently some Eastern European unionists have begun to defend their requirements by a reference to the European Social Model having in mind its inefficient continental form (or in another hidden modification referring to the average Eurozone figures with prevailing 90% GDP weight of countries with continental model) . It is beyond any doubt that by definition, the implementation of the inefficient Continental European social model promoted by some trade unionists, with the support of the short-sighted (mostly left-wing) governments, might undermine the competitiveness of the new EU member states and the goals of up-dated Lisbon agenda. In fact, the Continental model itself is currently under pressure to be reformed and some flexicurity model features are recommended policy in support of Lisbon agenda by some of EU policy-makers and by number of social democrats¹⁶. Some Nordic insiders themselves such as Munkhammar (2006, 2007) are criticizing how superficial and oversimplified judgements are made around Nordic countries and flexicurity model and show its current efficiency limits. The political agenda of number of several governments with long-term goals is pushing forward the policies with Anglo-Saxon model (even in Sweden). In fact the issues around European social (and economic) models are getting a highly political issue both at EU level and at national scale representing more and more the main agenda of political parties, one of the main stakes in the political struggle between the left and right – what should be the future models of capitalism accepted both by the member states and by EU as a whole¹⁷.

An interesting foreign policy example is a slogan which well illustrates this debate and that recently proved to be very effective. It was found on French billboards representing “Polish plumbers.” As a part of their May 2005 French campaign, opponents of the new European constitution struck fear into the hearts of French voters by conjuring an image of invading armies of low-wage “Polish plumbers” who would wrench jobs from hardworking locals. Hence migrating new member state citizens would capture old member state’s service jobs. Although there is a chronic lack of plumbers in Paris, voters overwhelmingly rejected the constitution.

¹⁶ See Spidla (2006) and number of recent EU policy papers. See also Enlargement and ESM Bucharest Policy network of Social Democrats Conferences (2006,2007).

¹⁷ See social democratic Dimensions of ESM (2007), On the other side the program of new centre-right wing Swedish government

As a response, the Poles have turned insult into opportunity. The Polish National Tourism Office launched a billboard campaign in France featuring a blond Pole dressed in plumber's overalls who declares: "I'm staying in Poland. Come visit." According to the tourism office, the ad campaign has been a huge success. The publicity campaign was "a humoristic wink to get people to visit Poland, but also a political wink at the Polish plumber ... who stands for the xenophobic feeling" said Pierre Lequiller, head of the French parliament's delegation to the European Union. In addition, in favour of the free circulation of workers within the framework of European bilateral deals, a campaign launched by the Swiss Socialist Party also features a similar character, with the slogan "Plumbers of the world, unite!" in reference to the famous slogan and last words of the Communist Manifesto, "Workers of the world, unite!" Finally, reflecting the empirical data that showed an excess of demand, the French "plumber sector" has been recently included among the first service sectors to open to international competition. This *volte-face* illustrates well the paradoxical development of topics relevant to the rigid, continental European Social Model and foreign policy issues within EU that could be easily extended to external foreign policies of some EU member states.

Rather than promoting phrases and slogans that lead to suspicion on the part of citizens, a sentiment which is to a large extent historically justified, there should be deeper analysis of the impacts of different elements of the social (and economic) models (recognizing the best practice from the worst practice not in the superficial indicators), leading to the consequent application of relevant policy measures addressing challenges different from the past within specific national framework¹⁸.

Eastern European countries must engage in a deeper public discussion of the pros and cons of various diverse social (and economic) models, while taking into account the effects of different social models on the past and future competitiveness of the countries that have adopted them. Rather than fixating on the past, they should assume a more forward-looking approach and allow those models to compete in the creation of new opportunities while maintaining full respect for the minimum harmonized standards (such as the social safety net). We have arrived to the same conclusion as recent pragmatic study of Canoy,Smith, 2006: "There is no inherent trade-off between social and economic policies, but to reconcile policies comprehensive modernization is needed". In addition, another crucial and relevant factor must be considered: the institutional framework of the bureaucratic burden should not only be reduced by „EU Better regulation“ policies, or incentives-oriented policies, on paper, but in reality as well.

As we have seen the globalization (including the growing role of Chinese supply and demand growth) increases competitiveness, international trade and structural change including the growing role of competitive service sector. It cannot be easily achieved only by current EU opening the tradables to foreign trade competition but also by rapid development of single EU service market

¹⁸ It still remains valid that people in Eastern Europe are a bit distrustful of political slogans, due to their experience with Marxist ideology. Citizens of these countries might perceive some elements of the debates on the European Social Model as echoes of the past. According to Singer (2005), in response to increasing economic problems within socialist countries, genuine Marxists experienced the following ideological development during the last century. Singer suggests that we are situated between the points 4 and 5.

1. Our idea is both right and superior.
2. The idea is right, but some errors occurred in its implementation.
3. The idea is right, but the wrong people are implementing it.
4. The idea is right, but the conception of the policies is wrong; however, when we change them, everything will be all right.
5. Everything is wrong, but the idea is right in principle.
6. The idea might not be as good as it initially seemed to be.
7. The idea itself is wrong.

that should trigger further productivity gains and not hamper the growth¹⁹. In any case the protection of numerous inefficient domestic service jobs is short-sighted and blocks spontaneous structural changes supported both by flexible labor markets and by more international competition and entry on the product markets, more investment in higher education and more developed internationalized financial sectors and markets (see Aghion, 2006). The responsible politicians should not be blind to the fact that historical features of still prevailing continental European Social Model are shared neither by Anglo-Saxon countries nor by the Asian dynamic economies (Chinese, Indian, South Asian) nor by the rest of world and try to update

As V.Semerak has shown in section 5 of the first part of Mejstrik,Chytilova,Semerak(2007), changes in the structure of production have been clearly linked to substantial structural changes. The fact that the former centrally planned economies started their effort aimed at increasing the standards of living of their population by introducing policies that contributed to increasing inequality and the reliance on the flexibility and mobility of labour during reforms sharply contrasted with traditional understanding of role of welfare state in original member countries. At the same time the welfare states of the same original countries were getting under pressure from increasingly globalized markets which led to discussions about reforms of their own welfare systems. Although Europe was experiencing problems even before reforms in CEE countries fully unfolded and the relative position of Europe in the world economy was not developing too well (see Section 2 of the first subchapter), in the eyes of many this pressure for changes coincided with the efforts to re-integrate the former socialist economies back to European economy. Many interest groups that feared possible impacts of the welfare reforms on their own status therefore started viewing even the reintegration of the newcomers as a threat. On the other hand, some of the measures suggested by the advocates of the traditional approach (restrictions to mobility of workforce, limited mobility of services, labour and social standards) could be rightfully viewed as a threat by the new member countries as the measures could restrict their ability to continue with reforms and structural changes as necessary.

As we said above, although there is space for mutual cooperation and discussion regarding the effectiveness of different aspects of national policies, which could possibly lead to deeper discussions about the direction and guidance of social policy measures, different approaches towards social issues and different cultural patterns among member states make it in many cases impossible to implement the most effective practices of one member state into the policy framework of another. However, it is possible to enact significant changes that counter the natural direction of social development when those changes are promoted by a strong and charismatic political personality that is able and willing to face the challenges of their uneven impacts. Different time horizon of rather remote benefits and the short-term painful impacts is usually amplified by negative impacts being highly concentrated within few regions or sectors. Intensive discussions about the benefits of different social models, taking into account both equity and sustainable efficiency is a certain guarantee that the appearance of a strong and charismatic personality will not result in the sort of populism that sacrifices the well-being of future generations for short-term comfort.

¹⁹ In that respect one could learn a lesson from Japan that experienced the similar problems with its competitive foreign trade of goods but protected inefficient service sector.

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Annex: Public Goods

According to its original definition, public goods fulfil two criteria: they are both non-rival and non-excludable, which means that the consumption of the good by one individual does not affect the availability of the good for others, and at the same time, it is not possible to exclude anybody from the consumption of the good. Since there is little motivation to provide a desirable quantity of public goods, their availability can sometimes be insufficient due to the free rider problem, and as a response, state ownership and full care for these types of goods is considered to be the most appropriate.

However, increases in technological development have narrowed the variety of public goods. For example, as a consequence of the implementation of electronic toll systems, highways have become quasi-private goods since it is possible to exclude consumers from its usage. In terms of the creation of the incentives in such cases, the regulation approach is often believed to be more efficient than state ownership and bureaucratic burden.

In addition, not only have technological changes affected the definition of public goods, but the process of globalization has as well. Global public goods were defined in the framework of the United Nations Development Programme. In a globalizing world, there has emerged a necessity for new methods of dealing with topics such as international air traffic control, peace and security, the multilateral trade regime, water management, biodiversity conservation and corruption control– all of which are perceived as global public goods.

Six priority global public goods as identified by UN are:

- Maintenance and enforcement of peace and security
- Control of the spread of communicable diseases
- Protection, preservation and exploitation of commons (biodiversity, natural resources)
- Improvement of global financial stability
- Open and fair international trading regime
- International policy coordination and consensus on issues of private intellectual property and knowledge in the public domain

A fundamental question raised in relation to global public goods is who should be entrusted with the decisions regarding multinational public goods specification and who should be charged with their maintenance. In addition, should a legal framework be included as one of the global public goods as defined by the UN? Is the definition of global public goods too broad?

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