JCMS 2005 Volume 43. Number 2. pp. 287–310

Converging Divergence: How Competitive Advantages Condition Institutional Change under EMU*

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Abstract

Recognizing that the institutional design of EMU leads to the co-ordination of national wage-bargaining structures, this article asks why bargaining systems in some EMU Member States have become co-ordinated and centralized, whereas others have become co-ordinated and decentralized. In contrast to neoliberal theory, it is argued that different bargaining levels are best explained by a country's competitive advantage: whilst countries with a competitive advantage in high-quality manufacturing favour a centralized bargaining system which supports a high-skill strategy, countries with a competitive advantage in low-cost production prefer decentralized bargaining structures which accommodate high wage differentials within the various employment categories of an industry. Thus, even though EMU asserts unilateral pressure for institutional change, it does not lead to the convergence of national institutions.

Introduction

On 1 January 1999, 12 of the then 15 EU Member States replaced their national currencies with the euro within the framework of economic and monetary union (henceforth EMU). Among the most important consequences of this decision is the impact of the institutional design of EMU on national wage-bargaining systems. The Maastricht convergence criteria not only make EMU membership conditional on comparatively low domestic inflation rates, they also notably

* I wish to thank Klaus Armingeon, Paula Blomqvist, Colin Crouch, Pepper Culpepper, Jaap Dronkers, Bob Hancké, Anke Hassel, Christian Kascha, Markus Poschke, Martin Rhodes and Sanne Zwart for stimulating discussions and their comments on earlier versions of this article.

restrict the autonomy of national governments to conduct independent fiscal, monetary and exchange-rate policy. Thus, the only opportunity for national policy-makers to bring inflation rates into line with the Maastricht convergence criteria, and to maintain low and stable inflation rates once their country has joined EMU, consists in securing non-inflationary wage increases.

In response to the fact that incomes policy remains the only autonomous sphere of national macroeconomic policy-making, an extensive literature has emerged that analyses how the institutional design of EMU affects national wage-bargaining systems. Overall, this literature agrees on two points. Firstly, that EMU triggers a change in national bargaining structures. Secondly, even though disagreeing on the nature of the predicted outcome, the various strands of the literature agree that national wage-bargaining systems will ultimately converge throughout the euro area. Accordingly, EMU is supposed to lead either to the 'Europeanization' of wage negotiations at a supranational level (see Schulten, 2002; EIRO, 1999a), or to bargaining 'decentralization' at the company level (Burda, 2001; Martin, 1999). Alternatively, a third strand of the literature proposes so-called 'German wage leadership', in which the German trade union IG Metall continues to be the wage-setter for the entire euro area (Iversen and Soskice, 1998). A final – and, so far, most promising – analysis suggests that EMU entails the 'co-ordination' of wage-bargaining systems at the national level (Hassel, 2002, 2003; Hancké and Soskice, 2003).

To date, there is only very scarce evidence to support the ideas of wage-bargaining Europeanization, decentralization and German wage leadership. Instead, the 1990s witnessed a remarkable re-emergence of social pacts, which – in turn – suggests that co-ordination is the most likely outcome of wage-bargaining development under EMU (Hancké and Soskice 2003, pp. 27–34). To bring inflation into line with the Maastricht criteria, national policy-makers throughout the future euro area implicitly or explicitly urged their social partners to co-ordinate national wage-bargaining structures. Thus, in the course of the 1990s, the social partners in all EMU Member States concluded social pacts which resemble one another in that they secure co-ordinated wage restraint via the application of a strikingly uniform formula. This formula stipulates that wages shall increase within a margin determined by the sum of inflation (wage floor) and productivity growth rates (wage ceiling). In line with the Maastricht criteria, the application of this wage-co-ordinating formula not only insures national governments against inflationary wage settlements, it also reconciles the interests of trade unions in preventing real wages from falling with the interests of employers in maintaining international competitiveness by securing stable unit labour costs (see Hassel, 2002, pp. 158–62; Hancké and Soskice, 2003, pp. 34–40. In sum, it can legitimately be argued that the institutional design of EMU has led to the co-ordination of national wage-bargaining systems.

Yet, a striking empirical puzzle remains to be explained. Whilst national wage-bargaining systems throughout the E(M)U area have converged insofar as they became more co-ordinated in the course of the 1990s, a notable divergence (continues to) exist(s) with regard to the level at which wage increases are ultimately determined. In countries as diverse as Finland, Germany, Ireland, Italy and the Netherlands, co-ordinated wage increases are ultimately determined at the central level, whilst they are determined at a decentral level in countries such as Belgium, France, Luxembourg and Spain (Traxler *et al.*, 2001, pp. 114, 307). In other words, both co-ordinated centralization and co-ordinated decentralization can be observed among the EMU Member States (see also Soskice, 1990). This article aims to explain this divergence. More precisely, it asks why – given that the institutional design of EMU leads to wage-bargaining co-ordination – some wage-bargaining systems become co-ordinated and centralized, whilst other systems become co-ordinated and decentralized?

Probably the most widely diffused explanation for bargaining (de)cenralization is that proposed by neoliberal theory. This is an employee-driven explanation in that it perceives differences in the degree of wage-bargaining centralization as a function of trade-union strength (see Stiglitz and Driffill, 2000, pp. 334–9). However, this explanation can be criticized for overestimating unions' capacity to influence national policy-makers. Instead of serving the interests of unions, national policy-makers seem rather to be concerned with meeting the demands of employers who seek attractive locations for investment. Accordingly, this article proposes an employer-driven explanation, as it argues that differences in wage-bargaining centralization are best explained by national competitive advantage. More precisely, it is argued that, in countries with a competitive advantage in high-quality production, wage-bargaining systems become co-ordinated and centralized under EMU, as this accommodates an education and training system which allows employees to acquire highly specific skills. Countries with a competitive advantage in low-cost production, by contrast, adopt co-ordinated but decentralized wage-bargaining structures since the latter allow preservation of wage differentials within the various employment categories of an industry. This, in turn, supports low-cost production in that wages, and hence production costs, can be kept at the lowest possible levels because equally skilled workers need not necessarily be paid the same wages throughout the industry.

To illustrate this argument, the article is organized as follows: Section I proposes two rival hypotheses as to why both co-ordinated centralization and co-ordinated decentralization can be observed in the EMU Member States. Section II tests these hypotheses on the basis of three simple linear regression analyses. The results show that differences in the degree of wage-bargaining centralization are, indeed, best explained by a country's competitive advantage. Whilst these results reveal the relative explanatory power of the two rival hypotheses, they do not tell us how co-ordinated wage-bargaining (de)centralization actually comes about. To provide a more in-depth analysis of how EMU causes national wage-bargaining systems to co-ordinate and (de)centralize in line with their competitive advantage, Section III compares the development of Italian and Spanish wage-bargaining structures since the Maastricht Treaty. Section IV concludes.

I. Two Rival Explanations for Wage-Bargaining (De)Centralization

This section proposes two rival hypotheses as to why EMU has led to co-ordinated wage-bargaining centralization in some Member States, whilst it has brought about co-ordinated decentralization in others. It is important to note that these hypotheses apply to, and are tested on the basis of, all 15 EU Member States, even though Denmark, Sweden and the UK ultimately decided not to join EMU. However, the ongoing debate in the UK about the eventual adoption of the euro reminds us that these three countries have also made considerable efforts to comply with the Maastricht criteria in order to be in a position to join EMU at any time.

Before discussing the two hypotheses, it is useful to point out that the notions of 'co-ordination', on the one hand, and of 'centralization', on the other, are entirely distinct (Soskice, 1990). The concept of co-ordination 'refers to the degree of intentional harmony in the wage-setting process – or, put another way, the degree to which minor players deliberately follow along with what the major players decide' (Kenworthy, 2001, p. 75). Accordingly, it is characteristic of co-ordinated wage-bargaining systems that they produce relatively homogenous outcomes, i.e. homogenous wage increases. The concept of centralization, in contrast, refers to the level at which wages are ultimately determined. Importantly, the degree of centralization is a function of three key elements, namely the bargaining level itself, the share of the workforce which is covered by wage agreements at each level, and the degree of horizontal centralization (Kenworthy, 2001, p. 59). Thus, in contrast to co-ordination, the notion of centralization describes absolute homogenous outcomes, i.e. the extent to which homogenous wage levels can be found within an economy. Whilst employees in centralized systems are paid equal wages for equal skills, workers in decentralized systems can receive quite different wages even if they are equally skilled. By carrying out various correlation analyses, Kenworthy, (2003, p. 11; 2001, p. 87) shows that co-ordination and centralization are, indeed, independent concepts. If at all, only very weak correlations exist between the various co-ordination and centralization indicators.

In predictions regarding the development of wage bargaining under EMU, the co-ordination argument is superior in that it predicts the 'right' direction of change. Yet, the proponents of the co-ordination argument can be criticized for not distinguishing sufficiently clearly between the concepts of co-ordination and centralization. Therefore, their analysis usually falls short in one of two ways. Either the analysis is incomplete in that it considers only the concept of co-ordination. In other words, the respective scholars argue that EMU leads to wage-bargaining co-ordination. Yet, they to not consider at which level co-ordinated wage increases are ultimately determined (see Hassel, 2002, 2003). Or, proponents of the co-ordination argument lump the concepts of co-ordination and centralization together in that they portray co-ordination as a synonym of centralization. Accordingly, the respective scholars argue that wage-bargaining structures not only become co-ordinated but also centralized as a result of the fact that social pacts (including the wage-co-ordinating formula) have been agreed at the central level (see Hancké and Soskice, 2003, pp. 41–6).

It should be noted that both arguments in favour of co-ordination entail an assumption that EMU leads to the convergence of national wage-bargaining systems throughout the euro area (see Hassel, 2002, p. 169). Yet, this is far from the truth. Table 1 shows that an impressive divergence exists with regard to the degree of wage-bargaining centralization. Of all existing measures of wage-bargaining centralization, that by Traxler *et al.* (2001, pp. 114, 307) is among the most valid and reliable (Kenworthy, 2003, p. 15; 2001, p. 70). For three reasons, this measure is also the most useful for the purpose of this study. Firstly, it is a behavioural rather than an institutional measure. That is to say, it indicates at which level(s) wages are ultimately determined, rather than reporting the potential bargaining authority of each level (Kenworthy, 2001, pp. 70–5; Kenworthy 2003, pp. 7–10). Secondly, it is one of the most recent and, hence, one of the most sophisticated indicators. Accordingly, it captures all three elements which are central to the concept of (de)centralization, namely the bargaining level itself, the share of the workforce covered, and the extent of horizontal centralization. Finally, it is a time-varying indicator which is determined separately for each year.[1]

[1] It should be noted that the most recent available indices, calculated by Traxler *et al.* (2001), date back to 1998. Furthermore, Traxler *et al.* do not provide data for Luxembourg or Greece. To obtain data for these two countries and to update the existing data for the other E(M)U Member States, a careful analysis has been carried out on the basis of the most recent EIRO reports on wage-bargaining development in the E(M)U Member States (see «http://www.eiro.eurofound.ie»). In so doing, the classification schemes used by Traxler *et al.* have been followed meticulously. In most cases, the classifications for 2001 remain the same as for 1998 – except for Spain where a slight decrease in the degree of wage-bargaining centralization can be observed (see also Section III).

Table 1: Degree of Wage-Bargaining Centralization in the E(M)U Member States in 2001

E(M)U Member States	*Degree of Centralization in 2001*
Ireland	12
Finland	11
Germany	6
Italy	6
Netherlands	6
Portugal	6
Greece	6
Austria	5
Denmark	5
Sweden	5
France	4
Spain	4
Belgium	3
Luxembourg	3
UK	1.5

Scores of wage-bargaining centralization, as defined by Traxler *et al.* (2001)[a]	
1	Company and plant, with group-specific bargaining
1.5	Company and plant, with all groups and group-specific bargaining equally important
2	Company and plant, with all groups bargaining jointly
3	Combination of industry and company and plant, with group-specific bargaining
3.5	Combination of industry and company and plant, with all groups and group-specific bargaining equally important
4	Combination of industry and company and plant, with all groups bargaining jointly
5	Industry, with group-specific bargaining
6	Industry, with all groups bargaining jointly
7	Combination of central, industry, company and plant, with group-specific bargaining
7.58	Combination of central, industry, company and plant, with all groups bargaining jointly at central level and group-specific bargaining at all other levels
8	Combination of central, industry, company and plant, with all groups bargaining jointly
9	Central and industry, with group-specific bargaining
10	Central and industry, with all groups bargaining jointly
11	Central, with group-specific bargaining
12	Central, with all employees bargaining jointly

Source: Traxler *et al.* (2001, pp. 114, 307), updated as reported by the EIRO («http://www.eiro.eurofound.ie»).
Note: [a] The scores have been reversed so that the lowest score indicates the lowest degree of wage-bargaining centralization, and vice versa.

How can divergence in wage-bargaining (de)centralization be explained? Probably the most widely diffused explanation is that proposed by neoliberal theory which attributes differences in the degree of wage-bargaining centralization to a function of trade-union strength. As a rule, neoliberalists assume that unions prefer wage-bargaining centralization, whilst employers prefer decentralization because the monopoly power of unions, i.e. the capacity of unions to negotiate comparatively high wages for their members, is stronger in centralized than in decentralized bargaining systems (see Stiglitz and Driffill, 2000, pp. 334–9).[2] The reason is straightforward: in a decentralized bargaining system, where wages are determined at the company level, the monopoly power of (firm-level) unions is reduced, because the price-elasticity of product demand is lower for the industry than for a company. This means that increases in the workers' incomes directly affect the competitiveness of their firm. Excessive wage increases for some union members therefore result immediately in the dismissal of other union members. Thus, unions refrain from asking for excessive income increases with the result that wages are set at a market-clearing level. The opposite argument applies to centralized wage-bargaining structures (see Calmfors and Driffill, 1988).

This reasoning leads neoliberalists to argue that degrees of wage-bargaining centralization are importantly determined by the strength of the unions. The stronger the unions in a country, i.e. the more policy-makers rely on unions as partners in labour-market and economic-policy reform, the greater is the unions' capacity to extract concessions from national policy-makers so as to centralize the wage-bargaining system. Thus, from a neoliberal perspective, the different adjustment paths taken by the wage-bargaining systems of the E(M)U Member States during the 1990s are best explained by the strength of the unions in the early 1990s (see, e.g., Ewing, 2003, p. 21). This assumption allows us to formulate the first hypothesis to be tested in the course of this article:

H1: In countries where unions were strong in the early 1990s, the wage-bargaining system remained or became (co-ordinated and) centralized in the course of the 1990s, whereas it remained or became (co-ordinated and) decentralized in countries with weak unions.

However, this neoliberal, or employee-driven explanation can be criticized for attributing too much importance to the need for winning union support. Indeed, the experience of the UK in the 1980s shows that the national government was little concerned about alleged union strength. At the end of the 1970s, the British unions were highly influential, as they had traditionally been strongly involved in economic policy-making (see Traxler *et al.*, 2001, pp. 312, 76, as presented by Kenworthy, 2003, pp. 6, 27). Furthermore, as a consequence of the two oil crises, the need for unions' support in order to realize urgently needed labour-market and economic-policy reforms was particularly high. Yet, in line with the preferences of employers, the government did not care about the potential need to co-operate with unions but, rather, disempowered them by decentralizing the wage-bargaining system (see Hall, 1986, pp. 108–10).

[2] For a better understanding of this and following arguments, it is useful to specify that wage settlements are 'comparatively high', 'inflationary' or 'excessive' whenever nominal wage increases exceed the sum of inflation and productivity growth, i.e. whenever real wages increase above the rate of productivity growth. Since such wage increases are not justified by a proportionate rise in (inflation and) productivity, they lead to inflationary pressure.

Thus, national governments do not seem to be concerned about the preferences of unions – at least as long as they do not coincide with the preferences of employers. Indeed, it can be argued that the prosperity of an economy importantly depends on meeting the demands of employers who seek attractive investment locations, rather than on winning the support of unions (see Hall and Soskice, 2001, p. 45).

Accordingly, this article proposes an alternative, namely an employer-driven explanation for why EMU can lead to both co-ordinated bargaining centralization and decentralization. More precisely, the article suggests that the degree of wage-bargaining centralization is a function of the interests of employers to maintain or improve the competitive advantage of the economy. In line with Porter, two different competitive strategies can be identified, namely high-quality production and low-cost production (see Porter, 1985, pp. 11, 12–14). It is important to note that the capacity to pursue a competitive strategy successfully, and hence, the opportunity to obtain a competitive advantage in one of these two strategies, depends crucially on the degree of wage-bargaining centralization (Traxler, 1997; Estevez-Abe *et al.,* 2001; Soskice, 1999). While high-quality production and the manufacturing of customized goods requires a centralized wage-bargaining system, a decentralized bargaining structure is at the core of successful low-cost competition (Traxler, 1997, p. 31; Estevez-Abe *et al.*, 2001). The reasons are straightforward.

The manufacturing of high-quality products and customized goods depends crucially on a workforce with very specific skills. The centralization of wage bargaining plays a key role in enabling an education and training system that delivers the necessary skills, because it helps to convince both employers and employees to engage in sophisticated education and training programmes (see Hall and Soskice, 2001, pp. 24–5, 36–44; Estevez-Abe *et al.,* 2001). Employers invest in highly-specific training only if they are sure that their trained workers will not be poached by competitors. Centralized wage bargaining leads to the equalization of wages at equivalent skill levels across the national industry. Equal wage levels, in turn, reduce the risk of poaching, because workers are less likely to change a company if pay remains the same. For the employers this is an important mechanism to ensure that their investment in specific vocational training will pay off. In a similar vein, employees are willing to acquire highly specific skills, which are not easily transferable from one company to another, only if they are sure that such investment results in lucrative employment. In centralized bargaining systems, unions and employers usually negotiate not only wages but also training courses which, in turn, provide workers with very specific skills. The determination of training protocols, skill categories and professional diplomas, which are recognized by employers throughout the industry, ensures that specifically skilled workers can make use of their skills not only in the context of one company but across the whole sector (Hall and Soskice, 2001, pp. 24–5, 1999). Furthermore, the equalization of wages at equivalent skill levels (see above) assures workers 'that they are receiving the highest feasible rates of pay in return for' their commitment to invest in specific skills, which, in turn, motivates them to make such commitment (Hall and Soskice, 2001, p. 25).

In contrast to high-quality manufacturing, the success of low-cost production depends on a decentralized wage-bargaining system. Since the wage militancy of unions is reduced at the decentral level, a co-ordinated and decentralized bargaining system potentially allows for the lowest possible wage increases. Another important advantage of decentralized wage bargaining is that possible wage differentials within the various employment categories of one industry are not suppressed (Suárez Santos, 2002). In other words, workers with the same skills need not necessarily be paid the same wages. Although a political economy with a decentralized wage-bargaining system lacks the necessary institutional support to provide labour with highly specific skills, this disadvantage is secondary to the opportunity of maintaining high wage differentials, because low-cost production simply does not require highly skilled labour (see Estevez-Abe *et al.,* 2001, p. 175). In line with this reasoning, a second hypothesis can be formulated as to why the various E(M)U Member States differ in their degree of wage-bargaining centralization:

H2: Countries which had a competitive advantage in high-quality production in the early 1990s preferred their wage-bargaining structures to remain or become (co-ordinated and) centralized in the course of the 1990s, whilst countries with a competitive advantage in low-cost production preferred co-ordinated wage-bargaining decentralization.

Having formulated two hypotheses to be examined in the remainder of this article, the next section tests these hypotheses on the basis of simple linear regression analyses.

III. Centralized *v.* Decentralized Co-ordination

The above discussion has allowed us to formulate two simple hypotheses for why the wage-bargaining systems of the E(M)U Member States differ with regard to the degree of centralization. The question arises as how to operationalize these hypotheses? The indicator used to operationalize the dependent variable, i.e. wage-bargaining centralization, has already been discussed above (see Section I). Accordingly, the following discussion focuses on the indicators that have been chosen to measure the two independent variables, union strength and a country's competitive advantage.

Potentially, the strength of unions can be measured in a variety of ways, e.g. by considering the degree of union centralization, or union density rates (see Kenworthy, 2003, pp. 3, 6). Yet, for the purpose of the present analysis, we are not interested in the authority that unions have over their members. Instead, we are interested in the importance of unions for national policy-makers. Among the available measures of union participation in economic policy-making, the indicator proposed by Traxler *et al.* (2001, pp. 312, 76) is the most valid and reliable, as it is one of the most recent and most sophisticated measures. Furthermore, it is also the most complete in terms of the E(M)U countries it covers (see Kenworthy, 2003, pp. 6, 27). The indicator uses a range from 0 to 1 to express both unions' capacity to influence national policy-makers, and the extent to which unions are involved in the formulation and implementation of diverse economic policy programmes. Importantly, the indicator does *not* measure the degree of union centralization. Similarly, it also excludes all wage-related issues. This is important in that it prevents the neoliberal explanation from becoming tautological. In other words, wage-bargaining centralization is not explained by the degree of union centralization. Neither is wage-bargaining centralization explained by the authority of unions in the wage-bargaining process.

To measure a country's competitive advantage, one central assumption has to be made, namely that differences in prices (unit values) reflect quality differences. This assumption is not only central to macroeconomic analyses of trade patterns (see Commission, 1997, pp. 19, 41, 70–83), it is also supported by Porter, who argues convincingly that high-quality production is comparatively expensive, whereas low-cost production requires the reduction of prices at all costs (see Porter, 1985, pp. 127–8, 62–4). Accepting this premise, it can be argued that a country specializing in the production and, hence, export of high-priced goods has a competitive advantage in high-quality production. On the other hand, a country specializing in the production and export of low-priced goods can be said to have a competitive advantage in low-cost production. Thus, the competitive advantage of a country can be expressed in terms of the weighted relative unit value (henceforth WRUV) of its relatively most important export sectors.

Basically, the WRUV is calculated in two steps. In the first step, a country's relatively most important export sectors are determined by calculating the revealed comparative advantage (henceforth RCA). For each production sector, the RCA is obtained by comparing the relative export performance of a country to the relative export performance of a group of countries, e.g. the EU (see Balassa, 1965):[3]

[3] For a better understanding of how the RCA has been calculated, four points must be clarified: first, the data for calculation have been downloaded from the OECD online database 'ITCS – International Trade by

$$\text{RCA} = \frac{(\text{Exports of country A in sector p/Total exports of country A})}{(\text{EU exports in sector p/Total EU exports})}$$

The results obtained from these calculations show in which sectors a country has a comparative advantage, in that it exports comparatively more than the EU average. Typically, the strongest export sectors of a country indicate in which type of production a country specializes. For each E(M)U Member State, the five relatively most important export sectors have been compiled.[4]

In a second step, the WRUV has been calculated on the basis of these five sectors. In a nutshell, the WRUV reports how many percentage points average prices of the considered goods are above (or below) EU average prices. To obtain the WRUV, the relative unit value (henceforth RUV) is calculated by comparing the unit prices of a country's sector to EU unit prices in this sector:

$$\text{RUV} = \frac{\begin{gathered}(\text{Value of exports in sector p of country A}/\\ \text{Quantity of exports in sector p of country A})\end{gathered}}{\begin{gathered}(\text{Value of EU exports in sector p}/\\ \text{Quantity of EU exports in sector p})\end{gathered}}$$

As pointed out above, the RUV has been determined for each of the five relatively most important export sectors of a country. Finally, the WRUV is obtained by calculating the weighted average of these five export sectors.[5] What do these results tell us? Accepting the initial assumption that differences in prices (unit values) reflect quality differences, it can be argued that countries with a WRUV above 0 have a competitive advantage in high-quality production, whilst countries with a WRUV below 0 have a competitive advantage in low-cost production.

Table 2 summarizes both the strength of trade unions and the competitive advantage of the 15 E(M)U Member States in the early 1990s. The year 1992 has not been chosen arbitrarily as a reference year: in the early 1990s, the OECD changed the classification system of production sectors from SITC 2 to SITC 3. Thus, 1992 is the earliest year after the Maastricht conference for which export data can be obtained according to the updated classification

Commodity; SITC Rev.3' (available at: «http://www.sourceoecd.org»). Second, all export figures required to calculate the RCA are expressed in value (rather than in units). Third, the RCA has been calculated for all secondary, i.e. production sectors (SITC classes 5–9) because differences in the skills of workers have a notable impact upon the quality of manufactured goods, whereas they are unimportant for the quality of agricultural goods. Accordingly, primary, i.e. agricultural sectors (SITC classes 1–4) have not been considered. Finally, the considered SITC-classes (5–9) have been detailed to the 2-digit level.

[4] This equals roughly 12.5 per cent of all considered manufacturing sectors.

[5] The average has been weighted by comparing a country's exports in one sector (expressed in value, not quantity) with the country's total exports.

Table 2: Union Strength and Competitive Advantage of the E(M)U Member States in 1992

E(M)U Member States	*'Union Strength' (Union Participation in Economic Policy-making in 1992)*	*E(M)U Member States*	*'Competitive Advantage' (Weighted Relative Unit Values in 1992)*
Austria	1.00	Ireland	1498
Belgium	1.00	France	122.5
Denmark	1.00	Denmark	47.9
Germany	1.00	Sweden	43.9
Netherlands	0.92	Germany	24.0
Portugal	0.92	Italy	17.2
Finland	0.85	Belgium	15.9
Italy	0.85	Luxembourg	15.9
France	0.81	UK	10.2
Ireland	0.81	Finland	2.1
Sweden	0.62	Austria	–6.7
Spain	0.39	Spain	–11.7
UK	0.00	Portugal	–12.4
Greece	Not available	Netherlands	–23.5
Luxembourg	Not available	Greece	–26.2

Source: Traxler *et al.* (2001, pp. 312, 76); data provided by Bernhard Kittel.

Source: OECD (Online Database) 'ITCS International Trade by Commodity; SITC

scheme (SITC 3). In order to obtain comparable results, 1992 has also been taken as a reference year to report the degree of union strength. Table 2 shows a remarkable variety with regard to both union strength and the E(M)U countries' competitive advantage in the early 1990s. Thus, in line with hypotheses 1 and 2, the question arises whether it is union strength or, rather, the competitive advantage of a country that explains today's (de)centralization of national wage-bargaining systems?

To answer this question, three simple linear regression analyses are carried out. The first analysis (model 1) merely assesses the impact of a country's competitive advantage on the degree of wage-bargaining centralization. Similarly, the second analysis (model 2) tests the effect of trade-union strength. Finally, the third analysis (model 3) assesses the joint impact of competitive advantage and union strength on wage-bargaining (de)centralization. Table 3 summarizes the results. Model 1 provides strong empirical support for the second hypothesis (H2) formulated in Section I. If it holds true that today's differences in wage-

Table 3: Results: Impact of Competitive Advantage and Union Strength on Wage-Bargaining (De)centralization (Standard Errors in Parentheses)

Independent Variables	*Model 1*	*Model 2*	*Model 3*
Competitive advantage	0.623**	–	0.612***
	(0.002)		(0.001)
Union strength	–	0.364	0.344
		(2.638)	(2.072)
Constant	5.053***	2.660	2.318
	(0.607)	(2.176)	(1.712)
N	15	15	15
R square (R^2)	0.389	0.132	0.506

Source: Author's own data.
Note: Significance levels: * < 0.10 ** < 0.05 *** < 0.01 (2-tailed tests).

bargaining (de)centralization materialized because employers pushed for bargaining structures in line with the economy's competitive advantage, we should find a strong correlation between the competitive advantage of the E(M)U Member States in 1992, and their degree of wage-bargaining centralization in 2001. This is exactly what is shown by the first model. R^2 reports that 38.9 per cent of variations in wage-bargaining centralization can be explained by the competitive advantage of the E(M)U Member States in the early 1990s.

Model 2 tests the first hypothesis formulated in Section I. If it is correct that, in the course of the 1990s, strong unions found it easier than weak unions to make national policy-makers meet their demands for wage-bargaining centralization, we should find a noteworthy correlation between the union-strength scores of 1992 and the centralization scores of 2001. At first sight, model 2 seems to confirm this assertion, showing a moderate effect of union strength on the level of wage-bargaining (de)centralization. Accordingly, R^2 indicates that 13.2 per cent of variations in wage-bargaining centralization can be accounted for by union strength ($R^2 = 0.132$). However, the correlation between union strength and wage-bargaining (de)centralization is not significant, not even at a 0.182 significance level. Furthermore, in comparison to the employer-driven hypothesis (H2) tested above, the employee-driven hypothesis (H1) is a very weak explanation for wage-bargaining (de)centralization. In sum, both the weak explanatory power and high significance level of the employee-driven explanation suggest we should reject our first initial hypothesis (H1): different degrees of wage-bargaining centralization cannot be explained by union strength.

But what is the joint impact of union strength and competitive advantage on wage-bargaining (de)centralization? Most importantly, model 3 shows that no correlation exists between the two independent variables, as the standardized ß of both the competitive-advantage and union-strength index remains virtually the same. In other words, union strength, on the one hand, and a country's competitive advantage on the other are two independent explanations for wage-bargaining (de)centralization. Furthermore, model 3 confirms the individual results of model 1 and model 2. The employer-driven hypothesis (std. ß = 0.612) far outperforms the employee-driven hypothesis (std. ß = 0.344) as an explanation for wage-bargaining centralization, whereby the results obtained for the latter hypothesis are not significant ($p > 0.10$). In sum, whilst the results obtained refute the neoliberal or employee-driven hypothesis (H1), they confirm the employer-driven hypothesis (H2). Thus, wage-bargaining (de)centralization is best explained by a country's competitive advantage.[6]

The results of the above regression analyses suggest that employers have been the driving force behind wage-bargaining (de)centralization in the E(M)U Member States. Yet, whilst the results indicate a strong correlation, they do not tell us how wage-bargaining (de)centralization actually comes about. In other words, which causal mechanisms lead to co-ordinated wage-bargaining (de)centralization under EMU? In order to show that employers, rather than unions have been driving the (de)centralization process, the following section compares the development of wage-bargaining systems in Italy and Spain since the Maastricht conference in December 1991.

III. Centralized *v*. Decentralized Co-ordination – A Two-Case Comparison

To understand how co-ordinated wage-bargaining (de)centralization actually occurs as a result of EMU, a two-country comparison is carried out in the remainder of this article. For two reasons, Italy and Spain provide ideal-typical cases. Firstly, they are both critical cases in that EMU had a particularly strong impact on their national wage-bargaining structures in the course of the 1990s: due to their persistently high inflation rates in the early 1990s, Italy and

[6] This statement has to be qualified in two respects: firstly, it should be noted that the various country scores in both the competitive-advantage indicator and the union-strength indicator are not distributed entirely normally. To normalize the distribution of scores, the natural logarithm of both measures has been calculated. If the same regression analyses are carried out on the basis of these normalized values, the explanatory power of both 'union strength' and 'competitive advantage' decreases, as the values of both std. ß and R^2 decrease. However, it is important to note that, whilst these absolute values decrease, their relative explanatory power remains the same. That is to say, competitive advantage continues to outperform union strength as a significant explanation for different degrees of wage-bargaining centralization. Thus, the overall statements of the regression analyses remain the same. Secondly, Table 2 reports that the union-strength scores of Greece and Luxembourg are missing. To compensate for the missing cases, the scores of Greece and Luxembourg were substituted by the mean. The results obtained have been counterchecked by excluding the missing scores pairwise and listwise. It is important to note that, irrespective of these modifications, the absolute values of both std. ß and R^2 remained roughly the same. Accordingly, the statements of the above regression analyses were confirmed.

Spain were among those EU Member States that seemed least likely to fulfil the Maastricht convergence criteria in time to participate in EMU in January 1999. But, due to the co-ordination of their wage-bargaining structures, both Italy and Spain succeeded in bringing down inflation rates, and in entering EMU at its launch. Thus, of all the E(M)U Member States, Italy and Spain can teach us most about wage-bargaining development under EMU.

Secondly, Italy and Spain are ideal-typical countries for a two-case comparison in accordance with Mill's method of difference, as they resemble each other in many wage-related issues (see Mill, 1872, pp. 448, 451–2): in the early 1990s, the wage-bargaining structures in both countries were entirely unco-ordinated. During the 1990s, both countries followed a very similar adjustment path, from unco-ordinated wage bargaining to bargaining co-ordination. Furthermore, both the Italian and Spanish wage-bargaining systems seemed particularly resistant to reform due to highly politicized relationships between the national government and the unions. Despite these strikingly similar features, Italy and Spain differ with regard to their competitive advantage: whilst Italy has a competitive advantage in high-quality manufacturing, Spain is particularly competitive in low-cost production. Everything else being equal, this key difference explains why, in the course of the 1990s, the Italian wage-bargaining system became co-ordinated and centralized, whereas Spanish bargaining structures became co-ordinated but decentralized.

Before these adjustment processes are illustrated in depth, a brief outline of the competitive advantages of Italy and Spain is useful. Table 4 reports the relative importance and export prices (unit values) of the five export sectors in which Italy, and respectively Spain, have the highest RCA (revealed comparative advantage).

Table 4 reflects Italy's competitive advantage in high-quality production. In the early 1990s, the fashion industry (textiles, clothing and footwear) as well as the designer-furniture sector were among Italy's most important export industries. Interestingly, Regini reports that even during the economic crisis of 1992–93, these traditional manufacturing sectors showed continuous growth. According to Regini, the survival of these sectors has been possible due to the specialization of the Italian economy in high value-added production and in customized commodities (Regini, 1997, pp. 103–4). Indeed, Table 4 shows that, in 1992, the prices of Italy's most exported goods were decisively above the EU average. More precisely, the WRUV indicates that the most important Italian export goods were 17.2 per cent more expensive than the average EU exports in these sectors which, in turn, confirms Italy's competitive advantage in high-quality manufacturing.

Similarly, Table 4 reflects Spain's competitive advantage in low-cost production. The RCA indicates that, in 1992, Spain exported comparatively

Table 4: The Competitive Advantages of Italy and Spain in 1992

Five most Important RCA Export Sectors in Italy in 1992 (SITC Classes in (Brackets)	*Importance of Export Sector Compared to Total Italian Exports (%)*	*Revealed Comparative Advantage (RCA)*	*Relative Unit Values (RUV) (%)*
Articles of apparel and clothing accessories (84)	6.86	2.40	27.3
Footwear (85)	3.82	4.25	1.0
Furniture and parts thereof (82)	3.26	2.53	9.0
Leather, leather manufactures and dressed furskins (61)	1.17	3.50	5.1
Travel goods, handbags, etc. (83)	0.57	3.15	76.6
Total	15.68	Weighted relative unit value (WRUV)	17.2

Five most Important RCA Export Sectors in Spain in 1992 (SITC Classes in Brackets)	*Importance of Export Sector Compared to Total Spanish Exports (%)*	*Revealed Comparative Advantage (RCA)*	*Relative Unit Values (RUV) (%)*
Road vehicles (78)	23.11	2.03	–16.7
Footwear (85)	2.03	2.26	3.1
Rubber manufactures, n.e.s. (62)	1.81	1.79	–8.1
Leather, leather manufactures and dressed furskins (61)	0.71	2.12	73.8
Cork and wood manufactures (excluding furniture) (63)	0.63	1.23	17.5
Total	28.29	Weighted relative unit value (WRUV)	–11.7

S*ource:* OECD (Online Database) 'ITCS International Trade by Commodity; SITC Rev. 3'.

more goods than other EU countries in sectors such as leather, rubber and cork. However, these sectors were of minor importance to the overall Spanish export industry, considering that road vehicles accounted for 23.11 per cent of all Spanish exports in 1992. In other words, already in the early 1990s, the Spanish manufacturing sector was predominantly specializing in the production of road vehicles. Interestingly, Scobie reports that the Spanish car industry is without exception owned by, or associated with foreign automobile manufacturers who have out-sourced standardized production processes in order to enjoy still comparatively lower wage levels in Spain (see Scobie, 1998, p. 73). The WRUV of –11.7 per cent confirms the specialization of the Spanish economy in low-cost manufacturing.[7]

To show how the competitive advantage of a country influences the bargaining level at which wages are ultimately determined, the following discussion illustrates how wage-bargaining structures changed in the course of the 1990s, first in Italy and then in Spain. Shortly after the Maastricht conference, the Italian government acknowledged the necessity to decrease inflation rates radically. Accordingly, Italy's policy-makers proposed a pact to its Italian social partners. More precisely, this social pact intended to co-ordinate wage-bargaining processes which, up till then, had been fragmented and unco-ordinated. The central provision of the pact consisted in the determination of a wage formula according to which, every two years, wages are negotiated successively at two different levels. Firstly, pay is increased at the national-sectoral level according to the inflation target of the ECB (EIRO, 1999c). Secondly, wages can be topped up at the firm level according to the company's productivity growth rate (EIRO, 1998b).

It is important to note that, even though the Italian pay formula *de jure* provides for wage top-ups at the firm level, such productivity premia are *de facto* negotiated only in large companies. In small and medium-sized enterprises (SMEs), which constitute the vast majority of all Italian firms, productivity premia are rarely granted to employees. Thus, it is only for workers in large companies, making up roughly 20 per cent of Italy's working population (Drüke, 2000, p. 45; EIRO, 1999b), that income increases are actually negotiated at the

[7] Spain is a particularly interesting case in that it has specialized almost exclusively in the export of road vehicles. In comparison, all other Spanish export industries are of almost negligible importance. Thus, except for the road-vehicle industry, a noteworthy discrepancy emerges between Spain's absolutely most important export sectors (calculated as: (Spanish sector p/total Spanish exports)), and Spain's relatively most important export sectors (calculated according to the RCA formula). This discrepancy explains why leather and cork, rather expensive export goods, do not notably increase the negative WRUV value. Yet, it is important to note that product prices in Spain's absolutely most important export sectors are far below the EU average. Thus, if countries' five most important export sectors were determined merely by comparing the absolute importance of the various sectors to the overall exports, rather than on the basis of the RCA, the Spanish WRUV would be even lower. Here, the RCA has been retained as a basis for calculation, because it offers a superior indicator of a country's export performance (see Balassa, 1965).

firm level. For the absolute majority of Italy's employees, working in SMEs, final income increases are determined at the central, i.e. the national-sectoral level (Callieri, 2002).

In July 1993, Italy's social partners accepted the government's proposal to co-ordinate the wage-bargaining process by applying the above-mentioned wage formula. Even though this led to temporary falls in real wages, the Italian unions agreed to the *de facto* centralization of the wage-bargaining system because it guaranteed their role as partners with both employers and national policy-makers. On the other hand, Italy's employers accepted the social pact because the centralized bargaining structure crucially supports Italy's competitive advantage in high-quality manufacturing (see Callieri, 2002). As noted above, a centralized wage-bargaining system supports a high-skill strategy in that it helps to convince both employers and employees to engage in highly specific education and training. Accordingly, Italian employees are willing to acquire specific skills because unions and employer associations at the central level have established industry-wide recognized diplomas which are awarded to trainees after they have passed exams at the end of vocational education programmes. Once they have completed vocational education, employees in Italy are, however, expected to update their knowledge through attending further training courses provided by their companies (EIRO, 1998a). At that stage, the fact that equal wages are paid for equivalent skills helps to convince employers to invest in specific training programmes, because the equalization of wages at equivalent skill levels reduces the risk of poaching. Indeed, the fact that equal pay levels reduce the risk of poaching is an important reason why even SME employers (collaborating in the production of customized manufacturing in so-called 'industrial districts') provide continuing training – often by combining their efforts in order to develop highly specific training courses (see Drüke, 2000, pp. 45–6; Callieri, 2002). In sum, employers in Italy have had a vested interest in an industry-wide centralized wage-bargaining system (see Estevez-Abe *et al*., 2001, pp. 147–9).

Interestingly, the social pact of 1993 was renewed with no noteworthy modification in 1998 (EIRO, 1999c). Furthermore, after its victory in May 2001, the newly elected right-wing government under Silvio Berlusconi issued several proposals to make the labour market more flexible. Strikingly, no provision touched on the wage-setting system or proposed its decentralization according to the Anglo-Saxon model (EIRO, 2002c). This confirms the idea that bargaining centralization is promoted by employers, rather than by the unions, as it seems highly unlikely that Berlusconi's government would have abstained from decentralizing the bargaining structure if centralization was merely in the interest of unions.

In contrast to their Italian counterparts, it took the Spanish social partners nearly ten years longer to agree on the co-ordination of national wage-bargaining structures. In 1992 and 1993, Spain's social partners rejected a government proposal to introduce wage restraint through an overarching incomes policy accord. At that time, the opposition came mainly from the unions, who were afraid that wage-bargaining co-ordination would – at least temporarily – lead to real wage losses (Pérez, 2000, p. 443). Spanish employers were certainly in favour of wage restraint. However, they feared that the co-ordination of wage-bargaining structures might entail the centralization of the system. This, in turn, was undesirable as it would have suppressed existing wage differentials within the various employment categories of an industry. Indeed, Figure 1 shows that, in the middle of the 1990s, wage differentials were more pronounced in Spain than in any other EU Member State for which comparative data are available (see OECD online database 'Labour Market Statistics'). Accordingly, Spanish employers have traditionally preferred a decentralized bargaining system (Suárez Santos, 2002).

Furthermore, until the mid-1990s, potentially higher and more inflationary wage increases resulting from the unco-ordinated bargaining system could be offset by competitive devaluation. Indeed, the peseta was devalued four times between 1991 and 1996, thereby strengthening Spain's international competitiveness substantially (Scobie, 1998, pp. 12–13). Thus, in the early 1990s, neither employers nor employees were interested in the centralization of the Spanish wage-bargaining system.

The situation changed after the completion of EMU, when exchange rate fixing precluded the possibility of devaluation in order to maintain the competitiveness of the Spanish economy. To ensure macroeconomic stability, the Spanish

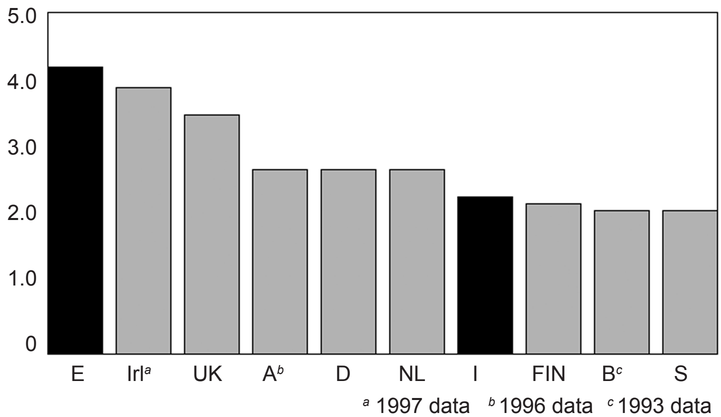

Figure 1: Wage Differentials in various E(M)U Member States
Source: OECD (Online Database) 'Labour Market Statistics'.

government – by threatening to impose a reform unilaterally – exerted pressure on the social partners to reach an official agreement on wage-bargaining co-ordination. Consequently, in December 2001, employers and unions agreed on a common wage formula according to which negotiators at all levels are requested to set wage increases in line with the government's annual inflation forecast. 'Wage increases [can however] be higher than the forecasted inflation rate within the limits arising from [productivity growth]' (EIRO, 2002b).

Interestingly, Spain's employers made sure that this co-ordination formula did not contain any obligations with regard to the prevailing bargaining level (Suárez Santos, 2002). Indeed, in line with the competitive advantage of the economy, wage negotiations in Spain still, and increasingly, take place at decentral levels (see CEOE, 2002, p. 6; EIRO, 2002a, 2004). In 2001, only 1.8 per cent of all collective agreements had been concluded at the national-sectoral level, whereas collective agreements concluded at the company level amounted to 73.5 per cent. Accordingly, the majority of the Spanish workforce is covered by agreements concluded at a decentral (i.e. regional, local, provincial-sectoral or company) level (EIRO, 2002a).[8] Thus, although co-ordinated, collective bargaining on wages continues to be highly decentralized. This not only entails moderate wage increases but also ensures that wage differentials are not suppressed within the various employment categories of one sector (Suárez Santos, 2002). In this way, wage-bargaining decentralization crucially supports Spain's competitive advantage in low-cost production.

In sum, comparison of the changes in the Italian and Spanish wage-bargaining systems since the early 1990s shows that divergences in the degree of wage-bargaining centralization are best explained by these countries' different competitive advantages. On the one hand, Italy's employers did not oppose the co-ordinated centralization of national bargaining structures, as this crucially supports the economy's competitive advantage in high-quality manufacturing. Spain's employers, on the other hand, made sure that the co-ordination process at the end of the 1990s did not lead to the centralization of national wage-bargaining structures, as this would have undermined Spain's competitive advantage in low-cost production. Thus, the two-case comparison of Italy and Spain supports the idea of the second initial hypothesis that wage-bargaining (de)centralization is a function of a country's competitive advantage.

[8] In 2001, about 71 per cent of the Spanish workforce was covered by collective agreements that had been concluded at a decentral level (EIRO, 2002a).

Conclusions

In line with the leading wage-bargaining literature, this article argues that the institutional design of EMU leads to the co-ordination of national wage-bargaining systems. However, in contrast to this literature, the present article finds that EMU does not lead to the convergence of national bargaining structures throughout the euro area. Instead, the outcome of changes in national wage-bargaining systems is rather diverging, in that both co-ordinated centralization and co-ordinated decentralization can be observed. Seeking for the origin of these divergent outcomes, a quantitative regression analysis and a qualitative two-case comparison have been carried out. Both types of analysis suggest that different degrees of wage-bargaining centralization are a function of a country's competitive advantage: in order to facilitate the training of highly skilled workers, countries with a competitive advantage in high-quality production prefer a co-ordinated and centralized bargaining system. Countries competing in low-cost production, by contrast, adopt co-ordinated but decentralized wage-bargaining structures, as the latter accommodate wage differentials within the various employment categories of an industry. These findings challenge the claims of neoliberal theory which portrays unions, rather than employers, as the most important driving force for wage-bargaining centralization.

Probably the most noteworthy implication of these findings is that one should expect institutional differences between high-quality and low-cost economies to become more pronounced as a result of EMU. As pointed out above, EMU not only brings an end to competitive devaluation but also increases the transparency of prices. Thus, an efficient production system becomes crucial if a company is to remain internationally competitive. Since wage-bargaining institutions can notably contribute to the efficiency and international competitiveness of national production systems, it is highly likely that employers will press for the most supportive institutional framework. Accordingly, it can be expected that wage bargaining in low-cost economies will become increasingly co-ordinated and decentralized under EMU, whereas economies specialized in high-quality manufacturing will opt for co-ordinated bargaining centralization. Thus, even though the institutional design of EMU exerts unilateral pressure for change in the (potential) Member States, this does not necessarily entail the convergence of national institutions.

Finally, it should be noted that the present study offers merely an initial assessment of how EMU triggers institutional change. More precisely, the arguments presented in this article invite further research in at least two respects. Firstly, these findings are based on a rather limited number of cases. The eastern European countries which recently joined the European Union provide potential additional cases. Thus, once these countries decide to join EMU, it will be interesting to analyse whether their national wage-bargaining systems follow the predicted adjustment path. Secondly, if it is true that wage-bargaining systems, on the one hand, and education and training system, on the other, are closely linked (see Hall and Soskice, 2001, pp. 17–33), changes in national wage-bargaining structures should have had profound impacts on national training systems. In other words, those countries which found themselves trapped in an in-between situation, in that unco-ordinated wage-bargaining structures neither supported high-quality nor low-cost production in the early 1990s, can be expected to have reformed their national training systems profoundly when their bargaining structures became co-ordinated and (de)centralized in the course of the 1990s. Thus, it remains to be seen to what extent EMU also induces institutional change in national education and training systems. It is, however, for future research to verify these assertions.

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