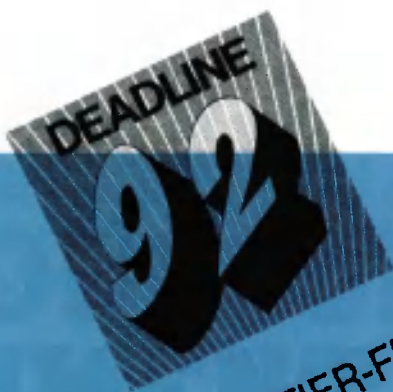


**PROGRAMME FOR RESEARCH AND ACTIONS ON
THE DEVELOPMENT OF THE LABOUR MARKET
YOUTH UNEMPLOYMENT POLICIES**



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PROGRAMME DE RECHERCHE ET D'ACTION SUR L'EVOLUTION DU MARCHE DE L'EMPLOI

YOUTH UNEMPLOYMENT POLICIES

FINAL REPORT

OCTOBER 1987

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SUMMARY AND CONCLUSIONS

This Report concerns how it has been dealt, and how to deal, with unemployment in Europe. This is the third of a sequence of Reports. The first one was based on the survey of four countries: Italy, U.K., GFR and France. The second one widened the evidence to Belgium, Greece, Ireland, The Netherlands and Denmark. In both cases the attention was focused, both in country surveys and in the general Reports, on the overall performance of the set of policies adopted in order to fight against youth unemployment. In other words, the attention was on the forest, rather than on the single trees and branches. Furthermore, the general Reports not only attempted a cross-sectional analysis of various countries, but were heavily integrated by analytical considerations about the systemic features of our societies on the one hand, and about the theories which were behind the adopted policies on the other.

The Report of this year, while extending its scope to two non EEC countries, Sweden and Austria, on one side consolidates the diagnostic side of the analysis, on the other one deals with a set of proposals, or, rather, a set of conditions which have to be fulfilled in order to attempt to revert the present unemployment trends in our countries.

The surveys on Sweden and Austria, which are attached to the present Report, partially differ from the other country surveys; our target was in fact to check whether very peculiar factors, having to do with the cultural, institutional and political environments, such as a different attitude towards cooperation, solidarity and planning, could have played a role in the management of unemployment problems. Therefore, we have not added these two countries to the comparative analysis performed in previous Reports; rather, we have used the knowledge about the two new experiences for deepening our analytical framework and, sometimes, we have gathered some policy suggestion.

The main results and conclusions of the present general Report can be summarized as follows.

(1) Youth unemployment is the apparent problem. The real one is unemployment. The inability to fully utilize available labour resources is the result of a deep crisis in the mechanisms of regulation, allocation and distribution.

(2) Such mechanisms worked relatively well until the early seventies. Since then macro-economic policies ceased to be effective. Expansive monetary stimuli started to produce increasingly price effects rather than real effects; more recently the possible breakdown in real and price effects of expansive stimuli has become substantially difficult to foresee. This amounts, in policy terms, to a loss of control of our economies.

(3) Inflation has become the main concern of our governments. The influence and leadership of the Ministries of Treasury in each of the countries has become overwhelming. This produced a reinforcement of the influence of economic advisors in the design of prevailing policies, and, thus, of the leading role of 'mainstream' economic theory.

(4) Economic theory is in a state of profound crisis, but the economists, for obvious reasons, tend to deny it and pretend that economic theory is not in such a state. In fact the policies which have been practiced since more than fifteen years have been successful (although very slowly) only in so far as the curbing of inflation is concerned; this was obtained, however, at the cost of a severe slowdown of the rate of growth, and at the cost of a dramatic and still increasing unemployment. Prevailing theories failed to give a real explanation of the changes which occurred in our industrialized economies around 1970. Their microeconomic foundations are completely deductive; since they are based on very simple and unchanging hypotheses of rationality, they are such as not allowing the analysis of the historical transformations, such as those which occurred in the last twenty years. The prestige which continues to be associated to such theories is due on one side to the high level of formal sophistication which has been reached by economic and econometric modelling, on the other one is based on the fact that the basic policy messages which are generated by such theories substantially correspond to what the political sphere is willing and interested to hear. A paradox like this is not new in recent history; it would be enough to re-read in such a perspective two books of John Mainard Keynes: 'The economic consequences of the peace' and the 'General theory'.

(5) We provide an interpretation of the changes which occurred in our economies around the first half of the seventies. This interpretation on one side explains the upsurge of stagflation and the increasing ineffectiveness of traditional economic policies; but it suggests also some of the directions in which to look for appropriate strategies to get out from the present crisis. However, to move in the directions that are suggested by our Report, requires a sharp change in the attitudes of policy makers. Two distinct factors militate against the likelihood of such a change: the first one is given by the cognitive attitudes of most of the political forces and of the mass-media from which the policy makers derive their strength, constituency and influence.

Such cognitive attitudes are such that (a) inflation is considered the worst of the evil; (b) promoting at any cost gains in the international competitiveness of the country is considered the best, when not the only, way to increase employment; (c) while everybody is ready to talk of the complexity which has been reached by our society, none is really ready to take it into account in the interpretation of facts and in the structuring of appropriate policies.

The second negative factor is given by the time specification of the interests and the constraints which affect the political sphere. The policies which are needed

imply long run perspective and a certain degree of intelligent generosity. The average time length of the political cycle is usually not long enough to allow policies aimed at pursuing relatively distant effects. On the other hand, the present economic strains and the paranoiac trend to international competitiveness are creating a climate, at the international level, which is favourable more to isolation than to an upsurge of solidarity and cooperation, that is, to what is now dramatically needed.

These considerations, together with those concerning the influence that economic theory is having upon policy makers, explains why we consider the need of changing the prevailing cultural attitudes as the main preliminary target, and why we devote a good deal of attention on one side to the criticism against the orthodox economic way to look at the present economic situation, and on the other one to the building up of a different interpretation of the major changes which have determined, and contributed to maintain, the present situation.

(6) The present situation can be summarized as follows. Our economies are heavily integrated. This implies that any action undertaken in one of our countries manifest spill-over effects in other integrated countries. This would require in itself more consciousness of the existing interdependence and more coordination in the actions. In some sense, it is as if we had become, at least within EEC, almost a unitary system, but this system continues to be led by different governments. However, this situation is made worse by the fact that all of the governments substantially share the same culture about policy making, and by the fact that the content of this culture is such that each one of the countries is convinced that the only way for being 'better off' is to gain something at the expenses of the others. Since each one of the countries behaves in this very same way, relative positions remain the same in the long run; all the gains are ephemeral; all of the countries end up in being worse off. In other words we are facing a negative sum game.

Before the Seventies the situation was different. Not only were the economies less integrated and interdependent, but the economic policies of the different countries were more differentiated and, above all, their business cycles and their counter-cyclical policies were less synchronized. Moreover, such policies were on the main more expansive, while each of the countries was on a path of building up an internal environment and climate of progressive social policies and social solidarity.

The abandonment of fixed exchange rates and the need to adjust to the first and subsequent oil shocks, dramatically changed, in the early Seventies, this favourable environment. In particular, the first oil shock obliged, for the first time, the different EEC countries to undertake restrictive policies at the same time; given the interdependence and the lack of coordination, the restrictive policies independently pursued by each country were made relatively ineffective by the fact that the same policies were adopted by competing partners; this brought to a reinforcement of the restrictive

policies themselves. This one was the first time in which the countries ceased to compete only on the ground of international trade, and began to compete straightforwardly in terms of macro-policies.

(7) The climate of slump generated by synchronized restrictive macro-policies generated a set of negative feed-backs in the national domestic environments. Such feed-backs can be summarized as follows.

- Companies changed their expectations. While until then they were quite confident in a relatively high and sustained rate of growth affecting quite homogeneously the different sectors, their state of confidence on the general business cycle began to be impaired. As a consequence of this, they started to rely increasingly only on the eventual positive expectations concerning their specific business branch. This led them to reduce, or even revert, the expansion of their productive capacity.

- This 'competitiveness drive' brought the firms to adapt their productive organization and technology to a more competitive, unstable and not forecastable environment. This produced a tendency to the reduction of the labour stock pertaining to single firms, to sub-contracting, to a search of flexibility based upon the externalization of many of the activities which were previously performed within the firms, with the contemporary building up of networks of separate firms; to the adoption of labour saving technologies.

- The search for competitiveness brought employers to reduce labour costs, not only acting upon gross wages, but also through the erosion of labour standards. This implied a change of personnel strategies and in the climate of industrial relations. The process was eased by a weakening of labour unions' strength, only partly due to growing unemployment.

There has been a strong, general and non selective reaction against public sector activities. This encompassed all of the state roles in the economy: allocation, distribution and regulation. This reaction found a fertile ground in the growing inefficiency and ineffectiveness of many of the public activities. The reaction tended to take the form of wild deregulation (also in the domain of labour and labour markets; many of labour policies amounted to bare deregulation), and of measures aimed at dismantling welfare state provisions; more in general it produced a loss of solidarity and coordination, and a general down-grading of ethic and cultural attitudes.

(8) The growing ineffectiveness of macroeconomic policies, coupled with growing unemployment, produced a stronger

fragmentation of different policies. On one side there was the set of budgetary and monetary policies; on the other one the remaining policies, above all industrial and labour policies, which took the form of remedial measures.

All these negative feed-backs contributed to make more rigid our economic systems and resulted in a reinforcement of the negative international interdependence.

* * * * *

From our analysis above of the current situation, some important policy implications follow; they are based on the need to take a new approach to policy. We have devoted chapter IV to develop these implications and what we regard as a coherent set of proposals and indications. We reproduce here a section of that chapter.

(1) The main policy implications are the following ones: labour policies, and in particular the youth unemployment policies which have been widely adopted by EEC countries, cannot but be fundamentally useless, since none of them is appropriate to deal with the set of problems which have been - in itself and within the present context - outlined. Some of the labour policies could result as useful, but only within the framework of an entirely different setup.

(2) No policy, if undertaken by a single country without coordination with the other connected ones, could obtain any relevant result. The main difficulty, however, is to push countries to collaborate and to coordinate themselves. Because of this, it is better even avoiding to attempt very wide inter-countries agreements, and to search for effective agreements among a limited number of countries, at least at the beginning. The ideal target would be to reach suitable agreements among EEC countries; but even a more limited coalition could constitute a good starting point.

(3) The most important target is to establish a climate of credibility about the undertaken policy arrangements. This, in turn, implies

(i) that the agreed structure of international coordination be credible; in order to have this, it should be better to root most of the countries' behaviours to clearly established automatic rules, that should be established through national laws before implementing the discretionary parts of macro expansive policies;

(ii) that the pursued expansion should be moderate and gradual;

(iii) that the pursued expansion should mostly be announced in real terms, that is, should be openly

translated in terms of programmes about 'things to be made'

(4) Macro policies should be supported and integrated by consistent micro policies, fostering the effects of the former upon the needed increase in productive capacity, while discouraging bets on prices and rewarding the firms that choose to expand their real output and employment. The structural design of such, entirely new, micro-policies will be actually described in section 6 below.

(5) The fifth implication is that the policy of coordination and cooperation at the international level should be replicated within the single countries. A new launch of strategies based on solidarity and of cooperation among otherwise conflicting parties would contribute

(i) to stabilize positive expectations, reinforcing the framework of certainties;

(ii) to corroborate the credibility of the adopted macro-policies;

(iii) to corroborate the climate of international cooperation.

This implies a strict collaboration/negotiation between planning authorities and social partners, in setting the likely and/or desired values of the main macroeconomic magnitudes, in stipulating the set of consistent behaviours to which the negotiating partners have to comply, and in defining the sanctions and the rewards of failure (the past Austrian experience is very suggestive in this respect)

(6) Macro policies should be integrated by additional policies, aimed at forestalling the idleness, and thus the deterioration, of labour and human resources in general, through special job-creation programmes. The feasibility criteria for the choice of such programmes should be agreed internationally, along the lines suggested in the previous chapter of this Report. For each individual there should be the guarantee that it should not be allowed that he could remain idle longer than a pre-established and clearly defined length of time; incidentally, this would contribute in itself to keep a favourable climate of expectations, since firms (as it is presently happening in Sweden) would read in that a serious plea, on the side of policy makers, towards a high level of employment and towards expansion.

(7) The extent of direct measures for special job creation programmes, and not only their evaluation criteria, should be agreed at the international level, since the fiscal adjustments, that such measures make necessary to adopt, could reverberate upon prices and, thus, upon relative competitiveness. Because of this, the best way, and the one to

be pursued in the longer run, would be to finance such measures by an increase in indirect taxes (value added, or an additional tax on consumption final goods), which would not be borne by exported commodities; however, this might be inconvenient in the shorter run, since it could contribute to develop a pressure on prices in the moment when expansive policies begin to take off, which would be undesirable.

(8) More in general the efforts towards expansion through macro-policies and towards additional employment programmes should be differentiated among country partners. The rule for such a differentiation should be established in advance and made to apply quite automatically. Such a rule should be linked to some indicators of the trend of trade imbalances within the group of countries participating to the agreement, so that the countries which tend to have a surplus in their balance of trade with respect to the others should be those which are bound to practice more generously both expansive and job creation policies. This attitude could become contradictory in the longer run, since such policies positively contribute to growth, welfare and productivity. It will be odd, thus, to limit the benefits that the weakest among the partners could get. However, it is a sort of 'must' at the beginning, when the risks and the possible costs, in terms of inflation and above all in terms of international imbalances, are higher. Because of the same reason it would also be better that the extent of such policies be larger for those countries which have a higher trade surplus and a lower rate of inflation in absolute terms.

(9) A good way for weakening the effects of the contradictions described under (8) would be that of reconverting the use of European funds, in such a way as to make more resources to flow towards the countries which have higher unemployment rates or infra-European trade deficits.

(10) A further important implication (the ninth one) is that the whole group of agreeing countries should aim at reflating the foreign demand for the goods produced within the area. This can be pursued by two coordinated sets of measures. On one side providing a system of guarantees and loans aimed at fostering the trade between the area and a relevant group of new developing countries. On the other one by promoting long term contracts between such countries and pools of firms belonging to different countries within the area.

(11) More in general, the whole of agreeing countries should promote a 'fair' degree of competitiveness with respect to the rest of the world, meaning by this the fact that the ability to compete should not be based, as it tends to be presently, on the erosion of labour standards and on the compression of wages, but rather on systemic efficiency, on the maximum exploitation of intelligence and culture, on well planned industrial coordination policies aiming at the valorization of the complementarities and synergies which appear to be potentially available within the European area.

(12) This requires to devote the maximum of efforts in favour of education and research, while deeply revising the presently prevailing tendencies favourable to low-profile training policies. Such policies, in fact, while possibly effective in the short run, not only reduce employment but contribute to render the system more rigid, since the tendencies towards continuous innovations tend to make rapidly obsolete any specific skill. Education, on the contrary, tends to render the labour force potentially more flexible and to mold the social environment in such a way as to become more creative and ready to accept innovations and their fruits. This does not imply the need to skip training activities, but rather that of avoiding to over stress their role and importance, that of shifting resources from training to general and higher education, that of rendering training vicarious to education.

(13) Many of the previous policy suggestions require a real leap in the quality of public action and, therefore, in intelligence and culture of public administration. Many of the suggestions imply also a widening of state intervention. Should the extension of the traditional sphere of state intervention and the quality of public administration remain as they presently are, the emergence of a negative attitude towards the proposed measures among ordinary people, mass media and politicians, would be likely to occur. This is why the whole of the proposed measures have not only to be accompanied by, but rely on, a profound revision of the philosophy of public action. The range of direct interventions should narrow, while that of regulation should widen; the state should directly make less things and become more capable to order to make things to third parties and to control that they properly and timely comply to such orders; in short, thus, less 'making', and more 'regulating and controlling'

CHAPTER I

THE CORE OF THE MESSAGE

1. Introduction

The present levels and trends of unemployment (and not just of youth unemployment) should raise a higher degree of concern and political alarm. In fact they are the manifestation of major forms of irrationality of our societies. Unemployment implies a loss of potential output. Furthermore, while there is still a wide set of unsatisfied needs (both private and collective), the people who could work for satisfying such needs are not only kept paradoxically idle, but are frustrated and suffer from material as well as psychological deprivation.

It is a subtle form of 'regulatory', if not plainly political, irrationality, that we overlook and to which we are beginning to be increasingly accustomed, while attributing the responsibility for it either to the forces of the system or, even worse, to the previous attempts to fight against them. However, human societies are not anarchic or spontaneous systems. Since their origins they have been characterized by their being structured by sets of rules and led by some form of government; and since the beginning of the present century many conscious attempts have been developed to impose some form of rationality on such rules and on the behaviour of the governments, as the end-result of long-lasting efforts, consolidated during the illuministic period and strengthened by recent cultural as well as factual 'revolutions', such as the blossoming of post-positivistic approaches, the explosion of mass education and the unprecedented economic affluence.

Political rationality is likely to be an endless escatological gamble. Nobody really thinks it could be achieved, and still most people believe it should be pursued; and that pursuing it is not only rational but positively contributes to some unspecified -but strongly shared- state of collective well-being.

Most of the social reforms that have been attempted, and partly achieved, in the course of this century -such as various forms of welfare state policies, post-keynesian full employment policies, the virtual elimination of extreme forms of poverty, the improvement of civil rights, etc.- are regarded as improvements in the degree of our political rationality, even by the majority of those conservatives who maintain critical attitudes towards the concrete features of such actions.

2. The subtle bias of 'scientific' rationality

Not only are most of these actions 'value loaded', those who have inspired them were 'value biased', such as Wickssell, Myrdal and the Swedish reformers of the early part of this century; as the Webbs, and Beveridge; as Roosevelt and the New Deal; as, though in a lesser degree, Keynes himself. This is why these fundamental steps in the history of our civilization were never truly regarded, within the scientific debate, as a real progress in the degree of rationality of our societies, despite the fact that for a long while most of the scientists were strongly influenced, if not even fascinated, by them.

But values are values and they are not regarded, by the highbrow neo-positivist tradition which prevails in social sciences, as being susceptible of evaluation from the viewpoint of rationality. So, for example, the value of solidarity can be liked or disliked, accepted or refused, but could not be considered as being more rational than that of aggressiveness and competitiveness.

It is to be noticed that such an epistemological attitude is historically new: classical economists -such as Smith and Ricardo- who considered the political economy as a part of their philosophical research, investigated the 'laws' of the economy in order to strengthen, with the help of rational investigation, their normative and ethical approach to better ways of ruling modern societies; and this tradition continued in economics until Pigou, that is, until the first quarter of this century, and then faded away, under the influence of apparently more 'pure' scientists, such as Pareto, Robbins and Hicks. It is to be noticed also that, paradoxically enough, such an epistemological attitude, while still dominating within the economic science, is now regarded as only instrumentally useful, but substantially obsolete, by most up-to-date philosophy of knowledge.

3. The need for an upsurge of intelligent solidarity...

There is a reason, a reason that we consider as most important for our Report, for devoting some attention to apparently peripheral issues in the history of economic and social thought. Present policies are in fact strongly influenced by economic disciplines; and particularly by those branches of economics which mostly departed from the classical and Pigouvian tradition. In their efforts to rule out value judgments, and to found a pure economic science, modern economics ended up in stylizing economic facts as determined only by the interaction of purely selfish individual motivations. Given this, no space exists, in the reconstruction of the world which is made by pure economists, for forces different from those which are motivated and put into motion by the selfishness of utility-maximizing individuals; that is, for forces which stem out of ethical and ideological motivations, from emotions and affective instincts, from moral intelligence, from the sense of

justice, freedom and solidarity, from the evolution of our aesthetic and moral as well as scientific culture.

As we said, the economic culture strongly influences our government leaders and opinion makers; therefore it strongly influences most of collectively relevant choices which are made in our societies. Quite on the contrary, we believe that what our societies mostly need, in order to solve their problems - of which growing unemployment is only the most visible and immediate one - is a new deal for solidarity, led by a renewed and long-sighted collective intelligence and culture.

Economics, in this respect, can become - and actually has become - more dangerous than a mere false description of the 'laws' which regulate individuals' behaviour. If economic systems and their laws of motion are not merely contingent on selfishness and utility-maximizing, any policy which, instead, is based on these assumptions will lead to long term failures rather than to the establishment of the 'true' economic (or social and political, for that matter) rationality.

Economic systems have always relied on some form of 'solidarity' (socio-economic compromises, policy measures aiming to blunt spontaneous contradictions, etc.). If we destroy those solidarity mechanisms in the name of a supposed higher form of rationality we may reach a situation in which every one is worse off.

The international arena is the clearest case: growth and development of single countries have always taken place in an essentially cooperative international environment. Highly ruthless competitive international environments have, on the contrary, always led to catastrophes, though in the short period some countries may have apparently made large gains (World War I - peace - World War II).

Thus solidarity is a value judgment but also a more concrete policy indication. We all should recall Keynes's attitude towards the peace-treaty after World War I (The Economic Consequences of the Peace).

Specifically, in our context, solidarity means finding expansive policies which could allow Europe to rise the global level of employment without single countries having to bear an excessive burden.

The above proposition is stated as a condition rather than a proposal. Our concrete proposals will be much weaker, although much more complex, such as to require a real leap in our ruling abilities. In fact the proposals will consist in an articulated set of provisions and rules aimed at coordinating internationally domestic actions to be developed by single EC countries. Coordination is thus treated as the first realistic step to be undertaken to establish a new wave of solidarity, not only within single countries but also among them.

4. ...despite the unfavourable cultural and political environment

Even so, it is not an easy task; on the contrary, it is likely to be over-ambitious, at least for the moment; a moment in which the wind of aggressive conservatism, of wild deregulation, and of over-stressed competition is powerfully blowing all throughout Europe.

And this is why the challenge to official and well established technical expertise becomes a difficult but unescapable preliminary task, despite the fact that policy and opinion makers tend to refuse analyses which are too demanding in terms of attention and comprehension efforts. And despite the fact that innovative cultural elaborations are disadvantaged in comparison with customary orthodoxy, since the latter tends to be accepted even if it is not fully understood, simply because of the persuasive strength which derives from well established conformism.

5. We are facing a negative sum game

General equilibrium models -the core of economic orthodoxy- represent the economy as a game in which the interaction among selfish players produces the maximization of the prizes which are available for the whole of the participating players. Our main point is that this could happen only under certain circumstances, which depend on the environment in which the game takes place and on the rules according to which the game is actually played; and both the rules and the environment are neither 'natural' nor 'fixed' by any standard of judgment. They are instead subject to change, along a sequential path in which the number and the quality of players, as well as the rules of the game and the resulting overall performances, influence each other. And the point is that present circumstances are such as to determine the prevalence and the likely extension of negative- sum games.

This is mainly due, though not only, to the fact that the competitive games, which were previously taking place mainly among individuals playing within fairly isolated systems, are now taking place also among systems; and while individuals compete (both within and across systems) under relatively stable rules, systems tend to compete each against the other through continuous and strategic adjustments of the rules themselves. It happens thus that the systemic results of the game drastically change.

6. The nature of the game depends on the environment

There is nothing, in what we just said, against the market as an acceptable and relatively efficient allocation mechanism. The market, however, is in itself nothing but a rule; and, like all rules, is neither perfect nor sufficient in itself, and its effects depend on the remaining rules which apply to the environment and on the features of the environment itself.

The market performed quite well until around 1970; that is, a period in which almost all of the EC countries were strongly involved in improving labour standards and developing ambitious social policies. Macro-policies were fundamentally expansive, and the climate of expectations was good. International monetary coordination, as produced by the agreements of Bretton Woods, worked in such a way as to ensure substantially stable exchange rates:

It was in this climate that international trade could develop, and the construction of the European Common Market could begin, despite the relevant range of the industrial and fiscal features which contributed to distort the competition among the European partners.

Then a sequence of events occurred that completely reverted the above picture. In particular a wave of aggressive competition began, which ended up with the countries competing each against the other in the field of restrictive macro-policies, through the worsening of labour standards and the dismantling of most of the previously adopted progressive social policies. Policy makers became increasingly concerned with inflation and less and less concerned with the issue of employment and labour standards, up to the point of indicating the improvement of labour standards as the main cause of inflation and rigidity. (This explanation, indeed, became the most appealing to opinion leaders, who never indulged in wondering how something -as the labour standards- which was so most different across countries, could actually be the cause of phenomena -such as inflation and unemployment- which were so similar in most of the countries.)

7. We must understand the transformations in order to regain control

Therefore, if we want to cure unemployment, we first have to attempt to explain, beyond prevailing superficial approaches, the complex process that produced the above described change. However, this is a necessary but not sufficient condition.

If -as we think- what happened was not a simple change in the values of variables and parameters of a basically unchanged structure, but a major structural change in our systems and in their reciprocal relationships, then the understanding of changes has to be integrated with that of the

actual working of the systems which resulted from these changes.

8. There is no easy way out

Our point will be that the degree of complexity and of uncertainty which characterizes our systems has grown much more and much faster than our ability to understand and govern them. Therefore, there is not any easy way out from the present problems; at least not one that does not imply a major change in the rules which are adopted, in the fashion of our collective life, in the culture and the skills which are used in the management of our systems.

We are still in a transitional phase. The unemployed are a minority, however great, but still a minority; they do not starve, nor are they violent. The degree of social alarm associated with unemployment appears to be now decreasing, and to rank rather low in the scale of political concerns. Most of the governments seem to be convinced that the problem is being solved automatically by demographic factors.

Not only do we not share these optimistic views, but we think that they are dangerous. Even if youth unemployment might actually decrease, this would not imply that we have understood and solved our problems. If, as we believe, unemployment is not 'the' disease, but just the visible symptom of it, and the true disease is the inability of managing and controlling our societies in a progressive way, the disease is bound to remain and to emerge, or to explode, somewhere else.

9. A sample of wrong answers

With this Report - as we said - we will accomplish three years of international research. Nine countries within the European Community and two outside (Sweden and Austria) have been considered. The financial constraints were such as to compel us to utilize second hand research, but strong efforts have been made to compensate this drawback by carefully targeting national contributions, through intensive coordination and active and extensive exchanges of ideas among the members of the international team.

We did not aim at a comprehensive collection of labour policies experiences nor at a careful microeconomic evaluation of them; we have chosen to maintain an overall and systemic perspective, and to focus upon the social, institutional and cultural differences which constitute the background of youth unemployment, and which thus make different not only what the occurrence of unemployment really means in different societies, but also help to explain how apparently similar provisions are differently conceived and actually administered, and tend to produce different effects in different societies. If, in fact, purely occupational overall

effects appear on average to be quite modest, labour policies appear to have, instead, quite relevant effects in other areas, such as social relations (family and households patterns, stigmatization processes,...), institutional changes (the role of training, the involvement of the sphere of education and the transformations occurring therefrom, the delegation of new tasks to local communities,...), the functioning of the labour market (new hiring patterns, new forms of labour segmentation,...), and industrial relations (the weakening of labour unions, the upsurge of concession bargaining,...), the personnel management strategies (restriction of the area of internal labour markets, new forms of labour organization,...), the distribution of incomes (between employers and employees, among employees, between workers and the rest of people,...). And many of these effects appear to have been somewhat negative.

Some of the attempted measures appear to have had positive occupational effects upon the directly affected youth; however, direct and indirect evidence tend to show that this is likely to depend either on what we could call a 'disguise' effect (people are induced to attend additional and special programmes for further training or education), or on heavy 'substitution' effects. Those who are hired because of the labour policies are actually squeezing out from employment some other people; and this perception is consistent with the feeling that the overall effects of labour policies are rather modest.

Such substitution effects put into light a rather new and worrying aspect of the whole issue: employment is becoming a new 'distributive' problem, similar but distinct from that of the distribution of income and wealth; distinct, in so far as the status of being employed is still, in our societies, a crucial, though too often overlooked, factor of social integration, and work is, for many, a source of satisfaction in itself.

When, during the second half of the seventies, youth unemployment began to worry the governments, most of European countries were still pursuing progressive policies in the domain of transition from school to work. The well consolidated German system -which was itself in the way of changing because of the implementation of previously conceived improvements- performed somehow, directly or indirectly, as a reference model. In countries such as GFR, Netherlands, Denmark, Belgium and France, the upsurge of youth unemployment tended to manifest itself as an ill-functioning of the mechanisms of transition from school to work. Many of the provisions which attempted to cure youth unemployment through the strengthening of the training efforts, and which were later on widely limited in other countries, were born in such a perspective.

This is a good example of the superficial, short sighted and naive attitude which policy makers, social parties and the vast majority of public opinion took with respect to the

problem. Since the more skilled had higher probabilities to find jobs, this was extrapolated to the system; unfortunately, what applies to individuals not necessarily does to the system, where the effects were simply a reshuffling of individual probabilities of finding jobs.

More sophisticated experts held that more training would have increased the relative competitiveness of the country. But since all of the competing countries did the same, relative competitiveness remained substantially stable, while the overall need for labour was likely to decrease.

Similar patterns of wrong conceptualizations stay behind other attempted measures, such as marginal employment subsidies and provisions aimed at fostering labour and labour-market flexibility. We call them, in our Report, 'stereotypes', since they have the look of common-sense reasoning, they are widespread among people and across countries, and they produce results which are very convenient for powerful vested interests.

Despite the great cultural, institutional and economic differences among the observed countries, the policy measures which have been adopted are extraordinarily similar, at least from a purely descriptive point of view. The only reason we have been able to find for this is the wide diffusion across countries of the same stereotypes. And this confirmed to us to put a priority upon the role and the inadequacy of the cultural endowments and of the ability to understand the functioning of our socio-economic systems upon which we are presently relying for regulating our societies.

10. Where we are with unemployment and labour policies

In this section we will attempt to summarize, in the most complete but compact way, as the end-result of our previous analyses, where we are - in Europe- in the domain of unemployment and unemployment policies:

(a) the problem is that of unemployment, not of youth unemployment. This is now becoming increasingly evident, as long as in some countries adult (mainly male) workers start to be squeezed out by (mainly female and/or young) workers. This was correctly forecasted, however, by our previous Reports, which pointed out

(a.1) that youth unemployment was only the most visible manifestation of a major allocation disease. This forestalls the use of idle (human) resources for the satisfaction of still unsatisfied needs;

(a.2) that, given the inability to raise the activity rate of our economic systems through aggregate economic policies, most of specific youth employment policies were likely to result in a mere redistribution of available jobs (see point c below);

(b) although some specific labour policies appear to have had positive effects, the whole of public policies, together with the associated consistent strategies adopted in the domain of industrial relations (increased labour flexibility and wage moderation), do not appear to have substantially alleviated unemployment problems, despite the fact that such policies and strategies have been actively and widely practiced all throughout Europe. Several hypotheses can be made for explaining such a failure:

(b.1) the theories upon which labour policies are based are plainly wrong;

(b.2) such policies (and the theories behind them) are correct only in so far as they succeed in affecting relative competitiveness; this could not happen because all of the competing countries adopted the same policies, reciprocally eroding the gains in competitiveness produced by the adopted policies;

(b.3) restrictive macroeconomic policies have compensated the hypothetical positive effects of labour policies.

In previous Reports -and in the second one in particular- we have argued that both explanations b.1 and b.2 apply (they are not inconsistent). As to b.3, it is certainly true that macroeconomic policies are among the causes of the unemployment situation, but not simply because they are -in the main- restrictive. The problem is that they have become substantially ineffective, so long as it cannot be established any longer a strict and mechanical correlation between a given budgetary or monetary expansive policy, a definite positive change of real GNP, and a definite increase of employment (this is nothing else than the 'other face' of what has been said under point b.1 above);

(c) the fact that labour policies and strategies have had some positive effects in lowering the specific unemployment of the directly affected population, while their overall effects have been poor or null, makes it clear their substantially redistributive nature. In other words, either such actions are ineffective or, when they are effective, this is due to the fact that those who are hired because of the policies are actually squeezing out some other worker. Since this overlaps with other forms of ongoing labour substitution processes, and the substitution effects which are produced by labour policies may be very indirect, it cannot be ascertained who is substituting whom (direct enquires have established, however, that youth policies are affecting employers' recruitment policies, while careful statistical estimates have shown evidence of substitution effects). Labour policies are thus not neutral from a distributive point of view; despite this, however, nowhere such policies appear to have been evaluated,

at the moment of their adoption, for their possible distributive effects;

(d) labour policies and strategies have produced or have been accompanied by, a deterioration of labour standards and welfare state provisions. This implied a redistribution of income and wealth, a redistribution that the theories which lay behind the adopted policies advocate as being what should be exchanged for obtaining more employment. While the redistribution has occurred, however, no more employment resulted from, and in exchange for, it. Quite on the contrary, all this appears to be producing not only a worsening of labour and life conditions of the most deprived part of the population, but also a disgregation of previous networks of social relations, and it is likely therefore to result in an overall impoverishment of the quality of human resources.

(e) New patterns of labour (and social) segmentation are produced. We find it convenient to single out six different groups:

(e.1) the highly paid, productive and stable workers. These tend increasingly to 'overwork', daily, weekly, yearly as well as during their life-time;

(e.2) the low paid, low productive but relatively stable workers. These tend to be concentrated in the public sector (of the majority of considered countries), and in other sectors which are sheltered from (mainly international) competition. It is within this group (but also within the previous one) that double jobbers are more likely to be found;

(e.3) precarious workers -mainly but not only young- who frequently alternate situations of employment and of unemployment. In other words these people have a high probability of finding as well as of losing jobs. Only a part of them succeed, after a period within this cluster, to move to one of the previous ones;

(e.4) the adult workers who lost their job, because of industrial restructuring or sectorial decline, and did not succeed in finding a new job within a short period of time. Usually these people did not rank very high in the job ladder, had very low or very specific qualifications, were female or elder workers. Such workers are among those who are most likely to be squeezed out by younger workers and as a consequence of youth employment policies;

(e.5) the young people who are socially stigmatized. The stigmatization could derive directly from social interactions (like in the case of poverty and

deprivation, and in the case of racial discrimination), or be due (or reinforced) by educational or training processes. Sometimes youth policies could paradoxically contribute to the stigmatization process. These young people get precarious jobs for short periods but face long spells of unemployment;

(e.6) the physically or mentally handicapped.

While we do not pretend that the above list is exhaustive, it is worthwhile to remark that many of the people within the groups outlined above may not belong to the labour force, according to the traditional statistical definition of it. In fact this definition is no longer sufficient to capture the whole of the people that, under different circumstances, would accept to work at prevailing pay conditions.

A second important observation is that the groups who face unemployment and social problems are, and are likely to remain for the next few years, minorities: dramatically relevant minorities, if considered from the viewpoint of the psychological conditions and the quality of life of the involved people, let alone the loss of potential output, but certainly minorities from a political point of view. And because of several reasons, such minorities are likely to have little or no 'voice' at all, which makes them a relatively uninteresting clientele from a political point of view, with possibly the only noticeable exception of cases of huge territorial concentration of unemployment, as it happens in traditional backward areas or in areas in which declining industrial sectors are concentrated (see g.4 below).

(f) In fact most of the European governments appear to have downgraded the priority of fighting unemployment; most of them appear to rely upon demographic self-adjustments. This attitude might result short-sighted, in face of the growing tendency of women to enter the labour market and to keep staying within it, and given the relatively low rate of female activity rates all throughout Europe and the growing tendency of employers to hire women.

(g) The phenomena considered above have been associated with, or accompanied by, relevant changes

(g.1) in the industrial strategies of firms. Largest firms decreased their employment, while new small firms were created, either independent or controlled by the largest ones. New networks of collaboration among firms have been created. The embodiment of new technologies, often labour saving, accelerated. Only smaller firms show a positive balance in terms of jobs creation;

(g.2) in personnel management and industrial relations strategies. Many firms are dropping the previously prevailing strategy of internal labour markets, while

others tend to narrow the scope and the range of application of them. A new prevailing pattern has not emerged yet, and it is not likely to emerge soon: while the need for flexibility and the search for cheap and disciplined labour push for a wider adoption of external labour market strategies, the high quality of technologies and, above all, the organizational complexity of the production processes might push in the opposite direction (these observations, however, which mostly apply to manufacture and to large and advanced service industry, must be reconsidered in the light of the changes occurred not only in the prevailing size of firms but also in the sectorial composition of economic activities). Correspondingly, labour unions strength and coverage tended to decline practically everywhere. Partly as a consequence of this, there has been a relevant wave of 'concession bargaining', according to which workers gave up not only shares of wage rates, but also many of the rights they had previously obtained in the sphere of working conditions (job security, job guarantees, seniority rights, etc.);

(g.3) in the sectorial composition of economic activities. Everywhere manufacturing activities declined in favour of services. Part of the phenomenon is somewhat spurious, since it is due to the fact that part of the service activities, previously performed within manufacturing industries, have been transferred to the service industry and are now bought from it; but part of it is genuine, and made for the invention of the new and rather queer expression of 'de-industrialization'. Within the enlarging activities, that of training has to be mentioned. Almost everywhere the number of people whose job consists in training activities has increased, both within firms and in the public sector, creating a network of vested interests around such activities;

(g.4) in the territorial distribution of expanding and declining economic activities. This makes for an uneven territorial distribution of unemployment rates, usually not compensated by labour territorial mobility;

(g.5) in the composition of public sector activities and tasks. Here the patterns are partly differentiated among countries, in the sense that the decline of welfare provisions induced in some countries a decline in the public employment in such domains, in others only a decline in transfer payments.

On the other hand, the most common patterns concern the fact that almost everywhere there has been either the creation of new agencies dealing with the various forms of labour policies, or the attribution of such tasks to previously

existing institutions, which thus had to reconvert themselves. In the latter case, often, the new asks have been additionally and/or improperly attributed -like when they were attributed to local authorities, which were not prepared or trained for them, without giving them a consistent set of juridical, financial and human resources- sometimes producing negative backlashes upon their efficiency in performing their ordinary institutional activities.

CHAPTER II

THE BACKGROUND

1. Introduction

In our 1986 Report we expounded and criticized in a very detailed way the features and the pitfalls of the presently prevailing macroeconomic models, using as a target for our critical evaluation the 1985 CEPS Report (O. Blanchard, R. Dornbusch, J. Dreze, H. Giersch, R. Layard, M. Monti, Employment and Growth in Europe: a Two-Handed Approach).

We consider those arguments as available to the Commission, and we will not return upon them here. However, we feel the need, on the one hand, to illustrate the major changes occurred in the macroeconomic background and in the macroeconomic policies around the first half of the Seventies and, on the other hand, to integrate our previous analysis by a better description of the basic rationale of the on-going strategies at the international level. We will accomplish this task in a synthetic way.

2. The early Seventies as a turning point

We consider 1972 and 1973 as the crucial years during which a sharp change in the structural functioning of our economic systems occurred. The events that we consider as crucial are the following ones: (a) the abandonment of fixed exchange rates, and (b) the first oil shock.

Notice that we do not consider such events as the causes of the major factual changes we considered in this chapter, but as the events which concluded an era and began new one; at the same time we consider such events as the catalyst of a transformation which was prepared by a sequence of events which had been occurring during the late Sixties. Furthermore, and obviously enough, we do not consider the present situation as close to that which immediately emerged after the events recalled above, but as the end result of a sequence of further adjustments and transformations that began with those events.

3. The mood of the Sixties

The sixties were the golden age of the Keynesian outlook. An unprecedented growth had been occurring in Europe since the late Fifties. In the first half of the Sixties all EEC countries reached what they considered as full employment.

The economy appeared to perform according to the theories of Keynes. The expansion of public expenditure or the money-supply invariably produced a growth of output and employment, with low effects upon the dynamics of prices and money wages. The new affluence produced a sharp increase in international trade. The common market framework in Europe was consolidated. European economies became increasingly interdependent.

Each of the European countries pursued a policy of stabilization which mostly concerned its own business cycle. The swings of the business cycles were generated mainly by internal events, such as investment cycles, wage drifts, etc. However, since the dependency upon international trade was growing, the equilibrium of the trade balances became increasingly important, acting mainly as an additional constraint upon the intensity of expansive policies. On the whole, however, the business cycles of each country were not fully synchronized. Furthermore, each country appeared to be positioned along a substantially expansive trend.

It is important to notice here that this positive attitude towards sustained growth, which was likely to heavily influence the mood of companies' expectations, by no means was rooted only to the prevailing macroeconomic philosophy. Quite on the contrary, this macroeconomic philosophy constituted an appropriate environment, within which specific progressive industrial and, above all, social policies were pursued, as the result of cultural and political attitudes and pressures. The need to fight against dualism and poverty, to get rid of various forms of underdevelopment enclaves, the need to strengthen the position of the weaker parts of the population, the need for improving labour standards and labour conditions, for providing better housing and transportation, for having more and better education, etc., were all felt and shared by a vast majority of people; and this was something which went beyond the contingency of the political majorities which existed in single moments in single countries.

Thus, it was this climate, such well rooted and diffused attitudes, that formed the basis both for expansive expectations and expansive policies. On the other hand, it is likely that expansive expectations created a tendency for the firms to widen their productive capacity quite in advance, creating thus a favourable environment to respond, rapidly and without strong tensions, to expansive policies by an increase of their outputs. Macro-policies confirmed the expectations of firms, and their success reinforced favourable attitudes towards their continuation.

These tendencies, that prevailed in each of the countries which were becoming increasingly interdependent, made for a positive circuit of interdependency among policies at the international level. In other words, although the need for equilibrium in the international trade acted as a new constraint, this did not produce excessive pressures towards sharp competition. If a country happened to be in a slump, while the other interdependent ones found themselves in a

relatively better position, this helped the first country to avoid a sharper recession. On the other hand, if a country happened to face an exceptional boom, the constraint of international trade could be cared for by the means of a moderate slow-down of growth, given the expansive trends of the other connected countries.

There was only one 'black cloud' in this happy landscape. It was given by money wage push, or drifts, due to full employment.

4. The model of the mood

Let us consider briefly how the situation considered above was stylized by standard economic modelling. The prevailing standard picture was given by what we could call the 'fix-price' Keynesian model. The economic system was represented as performing in the following way. Neither relative commodity prices, nor the ratio between money wages and prices, nor expectations, play any relevant role. The only thing which matters is the level of output which is demanded. The aggregate supply is perfectly elastic up to the level of full employment; beyond this, it becomes perfectly rigid.

A situation of equilibrium is characterized by the fact that the output which is produced in each period is fully sold. Selling all the produced (and therefore planned) output is a proof for the firms that their decisions about how much to produce were correct; therefore, such decisions are confirmed for the following period. There are no systemic or spontaneous reasons why this equilibrium output should be a full employment output. Therefore there can be unemployment. A situation of unemployment equilibrium tend to reproduce itself period after period. There is no reason, in fact, for the firms to revise their decisions. This is seen by the theory as being due to a sort of informational gap. If, in fact, all producers could be convinced to produce more and to hire more workers, this would determine an increase in the wage bill, and, as a consequence of this, in the level of final demand. And this increase in demand would match the increased supply.

However, no single producer would make by himself the decision to increase his output and to hire more workers, since this decision would not produce an increase in the demand for his own output. And each of the producers has the same attitudes. Thus, not only are the producers unaware of the systemic interdependency among a commonly shared decision to produce more and the aggregate consequence of this in terms of increased final demand, but, even if they had such an awareness, they could not have any guarantee that the decision to produce and hire more, made by one of them, would be followed by the remaining set of producers.

In such a situation, any public intervention aimed at increasing the final demand performs as an order, or a signal, conveyed to the economy. Newly produced money, introduced in

the economy by public spending, which has not at the beginning of a period a corresponding amount of output, amounts to an order, given to the producers, to produce the additional output which corresponds to the additional money; therefore, at the end of the period, increased money supply and increased output will match, without producing inflationary result. Any other intervention aimed at increasing private demand, like for example a lowering of the rate of interest through an appropriate increase of money supply and a consequent increase in the demand for investments, would perform a similar role.

That this modelling constitutes an emasculated image of the much richer environment described in the previous section could hardly be denied. However, the features and the possible roles of macroeconomic interventions are captured quite effectively.

European governments behaved 'as if' such a model actually captured the fundamental performance of the economic system, and this helped to maintain the economies along a fundamentally expansive trend and to pursue full employment.

The 'black cloud' of money wage inflation gradually began to overlap not only on the facts but on the modelling of them. The existence of an inverse relationship between the level of unemployment and a positive rate of wages and price inflation was first observed, and, later on, over-imposed upon the above described model (the so called Phillips curve). It is not by chance that for many years the Phillips curve was interpreted, by a causal point of view, either as a manifestation of a conflict of power between employers and wage earners (and their unions), which were considered as being reinforced by full employment, or as the manifestation of the effects of pure market forces; in this latter case, wage inflation was considered as the result of a normal demand pull in a situation of labour shortage produced by the proximity to full employment.

What it is worthwhile to be stressed here - since this has tended to be forgotten later on - is that in both cases wage inflation was strictly linked to the fact that full employment was a ceiling to demand expansion. In other words, the Phillips relationship, at least at the beginning, in no way altered the 'fix-price' nature of the basic model; it was only a sort of 'trap', which could be elicited by the fact of having reached the proximity of full employment.

On the factual ground, the emerging of inflationary pressures acted as a constraint upon expansive policies and produced an increasingly frequent interruption of them. We argue that it is extremely likely that such repeated interruptions heavily contributed to change the expectations of companies, slowing down the rate at which productive capacity was being built up. We consider it as equally probable that such a lowering of the rate of increase of productive capacity heavily contributed to make the aggregate supply increasingly rigid towards expansion, aggravating

inflationary pressures in the occurrence of expansive spells. This 'good sense' possibility was completely overlooked by prevailing analyses.

5. The shocks of the early Seventies and their consequence

At the beginning of the Seventies the international situation became suddenly quite turbulent. While the regulatory framework of Bretton Woods was fading away, the prices of many primary goods and raw materials, imported by most of industrialized countries (and, among them, by the EEC countries), began to rise; a sharp increase in oil prices was the end-result of a process started some years earlier, a process which was generated by socio-political factors which were in motion in the international arena, and in particular, within the North-South relationships.

In this new situation the external balance constraints acted upon the whole block of industrialized countries -and, in particular, on the EEC countries- in a way rather different from the past (see section 3 above).

Each industrialized country found itself in the need of readjusting, both rapidly and substantially, to the fact that the same amount of imported primary commodities, used as inputs in order to produce their output, costed substantially more than before. The required adjustment was very specific: the import of more expensive inputs could not be reduced but moderately, since it was necessary for producing final goods; the problem became thus mainly that of exporting more final goods towards the area of raw material producers and that of decreasing the import of final goods from other industrialized countries. The appropriate strategy was found, on the one hand, in the reduction of internal aggregate demand (both in order to reduce the import of final goods and in order to create an appropriate space for the export of final goods) and, on the other hand, in the pursuing of the maximum of competitiveness of national final goods (both in order to acquire a larger share of the imports of final goods made by the group of countries exporting basic primary goods, mainly OPEC country, and in order to export more toward the other industrialized countries, or to import less from them).

Therefore, the changes occurred in the international arena produced a situation in which all the industrialized countries adopted equal strategies in the very same moment. The business cycles, mainly induced now by government policies, became thus perversely synchronized, while restrictive macroeconomic policies became themselves 'competitive'. In other words, the restrictive policy adopted by each of the industrialized countries was weakened by the fact that the others adopted the same policy in the same moment. But the loss of effectiveness of each restrictive policy could only reinforce the intensity of the very same restrictive policy.

The imperative became, for firms as well as for governments, that of becoming more competitive than the others. Although it acquired a different set of meanings and implications for the firms, for the governments, and for the attitudes and behaviours of ordinary people.

For the firms it implied the beginning of a process of technological and organizational restructuring. This process was at the same time wide, deep and long lasting. Companies changed the strategies concerning industrial relations, hiring and upgrading procedures, and, more in general, personnel management. The division of tasks and roles between firms changed; larger firms started to reduce their employment, while the vertical integration of the production processes was diminished. Firms started to adopt strategies based upon the complementarity of network of different smaller firms. Labour-saving techniques were widely invented, through deliberate activities of research and development, and adopted. In many sectors the strategy of competition became increasingly based upon continuous innovation.

One of the aggregate result of this effort was a structural decline in the amount of imported primary goods. This contributed to re-establish a balance in the international trade, with respect to the countries exporting primary inputs. The restoration of more favourable terms of trade between industrialized countries and primary goods producers was partly the result of this structural adjustment and partly added its own effects to it.

The consequences upon government policies deserve more attention, since they are rather counter-intuitive. As we recalled earlier, the tendency of the terms of trade was, in the main and in the long run, to realign to the parity which existed before the first oil shock.

Governments on the one hand had to fight against a raising rate of inflation and, on the other hand, they had to promote the adjustments, considered earlier, to the new terms of trade between industrialized countries and raw materials and primary goods producers. In principle they aimed at obtaining this result through a mixture of restrictive and regulatory policies: increase of taxes, lowering of public expenditure, monetary restrictions, wage moderation. In practice governments met difficulties in lowering public expenditure; a good deal of the public expenditure, in fact, depended upon decisions undertaken many years earlier, during the period in which more progressive legislation was adopted and expansive expectations appeared to allow (and to reward, both economically and politically) generous public provisions and the growth of employment in the public sector.

Wage moderation was pursued because of two distinct but converging goals: controlling inflation and lowering the cost of labour, in such a way as to improve international competitiveness. In other words, the control of inflation and

external balances became everywhere the primary target of macroeconomic policy.

At the same time, the control of unemployment practically disappeared from the set of macroeconomic targets; even though many experts would not agree about the latter statement, since the official argument was that more unemployment in the short run constituted the strategy, and at the same time was the cost, to obtain more employment in the long run.

Without entering, in this chapter, into a critical evaluation of the arguments and the theories which stay behind such attitudes and behaviours, the situation described above manifests two paradoxes. As we saw, the drive towards a strong search for international competitiveness was generated by the worsening of the terms of trade between industrialized countries and primary goods and raw materials producers. But, once the game of aggressive competition had been put into motion, the game continued to sustain itself even when the terms of trade were re-equilibrated.

The second paradox is given by the argument of 'less employment today for more employment tomorrow'. The underlying thesis is that the country, increasing its competitiveness, could gain wider shares of the world market; less employment today would increase productivity and allow the gain. The obvious point is that what is important is relative, and not absolute, competitiveness. Since all countries are playing the same game, the relative competitiveness in the long run cannot be stable, and the only gains could be in the short run (which is the very same short run during which less employment is the mean to obtain higher competitiveness), and not in the long run, as it is instead claimed.

6. Some systemic negative feedbacks

As we saw earlier, restrictive macro policies resulted to be effective mainly in the fiscal and monetary sphere (apart from the regulatory actions aimed at moderating wage dynamics), much less in the sphere of public expenditure. In the latter one, however, the claims that public expenditure should be reduced continued to be conveyed as a signal to the economic agents, despite the difficulties to implement the asserted intentions.

All of the above actions were interpreted by firms as an unambiguous signal that the intention of the governments was not to allow either high rates of growth or long-lasting expansive cycles. As a consequence, the expectations were such as to lead firms not to enlarge, and possibly restrict, their productive capacity. Investments were thus concentrated on increasing the level of productivity and on substituting labour, rather than on the widening of capacity.

This produced further negative feedbacks. On the one hand firms were not interested in creating the conditions for

expanding production in response to the residual expansive stimuli deriving from the effects of a relatively high, although declining in its trend, public expenditure; therefore they tended to respond in terms of higher prices, contributing thus to maintain a relatively high rate of inflation, or, anyway, resisting to the pressure for curbing it. On the other hand the stagnation or the reduction of productive capacity contributed to create conditions of rigidity for the aggregate supply of commodities; this, in turn, created the conditions for a dynamic shortage of supply in face of expansive spells, and thus for inflationary pressures.

Both these effects fed-back upon the attitudes of governments, reinforcing their tendencies towards restrictive policies. The overall restrictive attitudes had further negative consequences. Many of the previously practiced public macro and micro policies had been conceived and practiced (therefore producing a learning process) in an expansive environment. Many of them, thus, had to be changed or substituted, others became ineffective, others, eventually, became contradictory.

All this contributed to raise the turbulence of the system and the degree of uncertainty about the future, reinforcing thus negative expectations and producing an overall climate of mistrust about the ability of the state to undertake effective measures and to regulate the system. The above described phenomena added up to a long run tendency to a growing ineffectiveness and inefficiency of State activities, about the causes of which we devoted some attention in our 1985 Report. Our arguments can be summarized as follows.

Most social policies were devised during a period in which there existed a relative homogeneity of people who constituted the main clientele of social policies. The transformations of society and its increased affluence were accompanied by a process of articulation and differentiation of social demands, aspirations and needs. Unfortunately, the tools of social policies failed to be updated in order to take into account such transformations. The flows of expenditures continued but their effectiveness decreased, and left people increasingly unsatisfied.

The second reason is the vicious circle of the procedures upon which the formation of the public budget is based. The major problem of those who are responsible for each line of expenditure is to maintain the ratio, or at least the level, of their financial resources through time. This, together with the concentration of the politicians' attention to the financial flows, contributed to the obliteration of attention to the substance of the actions and the concrete effectiveness of the strategies with respect to which the financial resources should be only a permissive factor.

Finally, spontaneous trends and the very same phenomena that we are describing conjured in fragmenting the political

clientele and, therefore, the interests which are cared for by the political sphere.

All this made for a cultural and political climate unfavourable to the regulatory activity of the state (while the demand for transfer payments, quite obviously, continued and was even reinforced by the deterioration of the economic and employment situation).

7. The conceptual models developed for the new environment

In this section we will consider briefly how the economists reacted to the challenges of the new environment described above. Theoretical thinking is characterized by selective abstraction. It is of extreme interest, thus, to examine the lenses through which the above scenario has been considered by influential economic thought.

While before the early Seventies the conceptual framework of general reference was basically unique (the fix-price Keynesian model), the following period is characterized by a flourishing of apparently differentiated approaches: neo-Keynesian models, neo-monetarist models, general equilibrium and rational expectations models. Besides such 'key-stone theories', there has been an extraordinary development of ad hoc applied modelling, mostly econometric. Furthermore, often the leading economists belonging to the 'noblest' schools recalled above, manifested their influence writing on the ordinary press; in such cases, however, they tended to use ad hoc arguments, quite far away from their abstract theoretical thinking and closer to the eclectic evidence accumulated within the set of applied economic analyses.

In our 1986 Report, we devoted much attention to the most important features which characterized the process of change, the transition from the old fix-price Keynesian model to the new set of leading models which declared themselves as inspired by the Keynesian thought. Using the CEPS' influential papers as a critical target, we outlined the main turning points of the theoretical transition and we demonstrated the anti-Keynesian nature of the final results. Therefore, we will not deal with the issue here. However, we will try here to outline the biases in the relationships models/facts of the various approaches, with regard both to economic interpretation and policy orientation.

Despite alleged differences, the main theoretical approaches have in common, a number of relevant features, the most outstanding of which is that in none of them the international dimension plays a crucial role. We do not say, by this, that such models do not allow for taking into account international interdependency; what we say is, simply, that the international dimension could constitute a complication, or a completion, of the model, but the performance of the model, which gives account of the phenomena upon which the interest of the model is focused, is already entirely determined by the structure of the relationships which stylize

the system as if it were a closed system. In other words, according to such models, we could have had exactly the same performances if our countries had continued to be only moderately dependant upon external trade and relationships, as it used to be until the Sixties.

The second important common feature is the common focusing of attention upon the causes of inflation. Unemployment, in all models, is something which happens to exist only in so far as something wrong happens with regard to price equilibrium. For the neo-monetarists the disturbing factor is given by an excess of money, for which the state is the direct responsible; for the neo-Keynesians the 'wrong variable' is given by the level of nominal wages (or of the nominal wages dynamics), which is too high. But in both cases, once the price equilibrium conditions are broken, unemployment will result as a consequence of it.

The third common feature is given by the common microeconomic specification of all these models, which pivot on the hypothesis of diminishing returns to scale. This point is crucial; so crucial that, should one withdraw the decreasing returns hypothesis, all of the main results of the above mentioned models would fail to hold.

In our 1986 Report we discussed this point at length; there we showed that Keynes himself accepted as an axiom such hypothesis but that his model, and above all his 'vision of the world', did not depend on it. In fact the Hicksian version of Keynes's model, and all the subsequent fix-price specifications, did not depend on that hypothesis. It was this, incidentally, which allowed to fit in such models more up-to-date theories of production and oligopolistic behaviour, which not only integrated the theory but contributed to make the whole building more realistic.

As we noticed several times, all the theories which at the moment dominate the academic arena have gone back to the nineteenth century microeconomic assumptions. The hypothesis of diminishing returns was borrowed by the agricultural process of production, to which it applied because of the existence of different land fertilities. Already the classical economists (and Ricardo is certainly the most representative of them from this point of view) assumed that industrial production processes had constant productivity with respect to the scale of production. The underlying consideration was that, should the productivity begin to decline beyond a certain scale of the plants, additional plants would be constructed, since in industry, differently from agriculture, productive capacity could be reproduced, at the same conditions, without any limit; industrial processes can be replicated, while land cannot.

The last common feature is given by the neglect for the numerous processes of innovation and transformation outlined in the previous section; more in general such approaches do not deal, and are not endowed to deal, with truly dynamic phenomena.

Neo-monetarist approaches have the merit of having reintroduced in economic analysis a relevant role for expectations. As a matter of fact, expectations played a very special role in the theory of Keynes; unfortunately post-Keynesian economists failed to acknowledge it, and in the fix-price tradition expectations did not play any relevant role.

Unfortunately, the neo-monetarist school narrows the scope of expectations to those about prices. If, as we said, factors such as complexity, lack of information and uncertainty, are the dominant features of the present environment, the fact of limiting the role of expectations to prices could not allow to build up any satisfactory explanation of what is happening.

Paradoxically enough, expectations do not play any relevant role in the neo-Keynesian model. Therefore, the sources of inflation and of its dynamics, are to be found entirely in the vicious spiral between money wages and prices. The whole of the neo-Keynesian point can be reduced to the fact that workers have lost the 'gift' of money illusion. According to Keynes, in fact, the workers could only negotiate about nominal wages, but were unable to act upon real wages; this was a fortune from a systemic point of view; since, due to it, increases of the aggregate demand could produce more employment and production, allowing, if necessary in order to offset the effects of diminishing returns, slight increases in prices (and therefore slight decreases in real wages), without putting into motion a price-wages spiral.

Once the hypothesis about the inability of workers to influence the real wages is removed, and it is therefore assumed that workers are able to bargain about real wages, the only way of expanding the output and the employment appears to these neo-Keynesian economists that of keeping under control the level of nominal wages. But this is exactly the target against which Keynes fought. In this sense it is difficult to consider these economists as Keynesian.

There would be nothing strange, however, in admitting that reality has changed, and that workers are now able to negotiate their wages in real terms. However, it would be interesting, in this case, to explore the conditions in which workers are able to do so, and how the changes of such conditions would influence it. The whole of neo-Keynesian arguments was developed under the influence of a period during which industrialized economies operated in the proximity of full employment. Later on, the employment situation deteriorated heavily, while, only partly as a consequence of this, the strength of the union decreased and the market power of workers diminished. However, this produced no feed-backs on the theoretical modelling.

This odd phenomenon can be explained quite easily (and we did it in our 1986 Report) as a consequence of having attributed a pervasive role to the pretended law of diminishing returns. Once it is assumed, as it is, that the

range of relevance of increasing costs with respect to the scale of production applies regardless of the absolute level of employment and exploitation of productive capacity, the very same concept of productive capacity fades away. In principle, a productive process appears to have no limits with regard to the amount of production that can be extracted by it, once the level of production is larger than that corresponding to minimum cost output; the output could be indefinitely increased, with any additional output costing something more than the previous one; and that is all. That is why the concept of productive capacity disappears. Quite on the contrary, the concept of productive capacity had a strategic role in Keynes's analysis, since it was only in its proximity that inflationary pressures could arise.

As we observed in our 1986 Report, the authors of CEPS Report hold that, since the late Seventies, it has begun a process of relative 'decumulation' of capital; in other words they hold that we are facing a lack of productive capacity. We consider this statement as being absolutely true, and we think that this intuition, given the influence of the authors, is extremely important.

However, it seems to us that this statement is made within an analytical framework which could not allow for it, given the above mentioned obliteration of any operative concept of full capacity.

Furthermore, it is obvious that we cannot agree upon the alleged causes of the decline of capital accumulation. If excess wages were actually responsible for it - as the CEPS economists hold - the adjustment processes which are described by them in terms of substitution of capital for labour, should have already produced a compensation for excessive nominal wages, through an increase in productivity. Therefore, excess real wages could not explain the lack of incentives to invest.

We think, on the contrary, that a problem of incentives exists, but it derives from the nature of prevailing expectations, and mainly depends on the perverse action of the governments upon them. This is why we consider as illusory the idea of promoting an expansion of capacity only through fiscal and monetary incentives, without any action aimed at molding suitable expectations.

Since the second half of the Seventies, both of the above recalled approaches tended to transform themselves in general equilibrium models. Each of the approaches carried its basic features with itself. However, the really new thing was an attempt to generalize the role of expectations, through the so called 'rational expectations theory'. We include such a theory in our critical consideration because of the implications that such an approach has on policies, as we will presently see.

The theoretical foundations of rational expectations theories can be summarized as follows. Given the uncertainty about the future, economic agents have to form expectations about it. The traditional hypothesis of rationality of economic agents is thus transformed in such a way as to assume that each agent has a 'model' to form his own expectations. However, since rationality is unique, people share the same 'best' model of the economy (a general equilibrium model with rational expectations). Not only will the agent form his own guesses about the future, but he can do so because he knows that the other agents have the same model and the same guesses. Each one will then know the future behaviours of other agents.

What is important is that people will have expectations about policy makers. In other words, elementary economic agents know which would be the policy undertaken by authorities in given circumstances and can, thus, adjust to them in advance. However, this amounts to say that policies have little scope.

This conclusion is substantially the same of that of the neo-monetarist, although it could be based on different grounds. A slight difference exists however. While within the neo-monetarist approach policies are not only useless but are the main responsible for our present disturbances and evils (and this is the triumph of 'laissez faire'), within the rational expectations framework there is still some room for policy making; but the only effective policy would be a 'surprise policy'; that is, a policy original (and irrational) enough to be a surprise for economic agents, displacing thus their (rational) expectations. It is intuitive, anyway, that this amounts to a radical narrowing of the scope for economic policy making.

There is still an important difference between rational expectations conclusions about policy and those of the neo-monetarist approach. While it is true that active policies are regarded by the latter approach as being not only ineffective but damaging, the recommendation that the neo-monetarists make to the monetary authorities about the need of announcing a given rate of money expansion and to stick to this announcement, is, in itself, a policy; a policy -notice- that highly stresses the problem of credibility on the side of policy authorities. While doing so, even if it is beyond their scope, neo-monetarists are actually ending up, paradoxically, with a new kind of policy, based uniquely upon a message of certainty with respect to economic agents. This point is important for us, since one of our main points will be about the need that the policy makers send credible signals to the economic agents.

We can now turn to the more heterogeneous knowledge constituted by applied economics and economic policy. A large part of it has been heavily influenced by the above recalled main theoretical lines. This explains why, also here, it is possible to notice certain recurrent features.

The prestige of the most fundamental schools makes for an eclectic view about the sources of inflation and the policies to take care of them. The responsibility tends to be attributed to both factors alternatively outlined by the main currents of thought: excess of expenditure and excess of money on one side, excess of nominal wages on the other. In both cases the attention is mainly focused on the financial flows which characterize the economy and about the 'arithmetics' of the rates of growth of nominal wages, labour productivity, prices and labour costs.

It is in this context that we find the propositions which are more adopted by governments, and, in particular, the ones which underlie the most adopted strategies of aggressive competition, which constitute the central critical target of the present Report.

We will devote to them a good deal of attention in the next chapters. However, the issue can be summarized as follows. The level of activity of the system is constrained by two kinds of possible disequilibria: inflation and external imbalances. Such constraints can be both removed through strategies that could keep the prices of domestic output lower than those of foreign commodities. Keeping the labour costs low and the productivity high allows to remove such constraints. It is possible that, in order to raise the level of productivity, choices have to be made that produce less employment in the short run; however, once sufficient increases in productivity have been obtained, the share of the world market dominated by domestic output grows, and this will produce a larger employment.

Other 'applied economics' or 'applied policies' positions are too contingent and differentiated to be dealt with here. The only thing that is worthwhile to be mentioned here is the fragmentations of conceptual frameworks underlying microeconomic policies, which is the mirror-image of the already noticed fragmentation of macro and micro-policies in the reality.

Many of the supported measures, such as training policies, marginal employment subsidies, temporary labour hiring and measures aimed at making the labour relationships more flexible, financial transfers to the firms to help their restructuring, have in general a broader scope than the one constituted by the increase in labour productivity and the lowering of labour costs; however they fit into the conceptual structuring of macro-policies only in so far as they 'appear' to increase competitiveness and to lower inflationary pressures.

This is clearly a short-sighted position, since a wider knowledge of the impacts of such measures could suggest that such provisions are not as effective as they appear at a first look, while a deeper scrutiny could show better approaches. There is, however, a second range of applied

economics which focuses upon the processes of production, the innovations occurring in this sphere, the labour segmentation, the problems of firms organization and reorganizations. Such researches have produced, since the last ten years or so, a remarkable amount of knowledge about the dynamics of real processes. However, since they do not fit either in the noblest theoretical approaches, or in the eclectic analyses influenced by them, they have not been embodied until now in a broader and more influential conceptual framework.

It is mainly drawing from this rich material, supported by a tremendous amount of empirical investigation, and based upon attempts to build broader theoretical frameworks starting from the evidence accumulated along this path, that the present Report has been mainly constructed.

CHAPTER III

KEY-STONES FOR AN ALTERNATIVE APPROACH TO THE PRESENT CRISIS

1. High productivity strategies and unemployment

Time has come to state in the simplest possible way the basic rationale of the problems we are facing. In order to do it without ambiguities, we shall support our considerations with extremely simple algebraic formulas.

The national product, Q , may be seen as the product of the average labour productivity, v (how much a worker produces on average per unit of time) times the number of employed workers, N :

$$Q = v N$$

Call N^* the number of workers corresponding to full employment;

$$Q^* = v N^*$$

would thus be the maximum possible output of our society.

We have unemployment, presently, in our societies. Therefore we have an output which is less than the maximum possible one:

$$Q = v N < Q^* = v N^*$$

The fundamental reason which is alleged for this, and that pushed the governments to adopt the presently prevailing policies, is that such policies improve the competitiveness of the countries which adopt them, raise their average productivity, and therefore their national product. It is admitted that the choice of a competitive path could produce unemployment in the short run; but this is regarded to produce more employment in the longer run, since it is held that the gains in competitiveness will enlarge the national shares in the international world trade.

We can think of the problem as if one could select among two different strategies. Strategy 1 (S_1) would ensure full employment, while strategy 2 (S_2) would not be able to obtain this result, but it would produce, however, an average productivity, v_2 , higher than that of strategy 1, v_1 ; higher enough -it must be added- to ensure that the national product associated with such strategy, Q_2 , could be larger than the national product associated with strategy 1, Q_1 , despite the lack of full employment:

$$Q_2 = v_2 N_2 > Q_1 = v_1 N^*$$

[1]

Obviously $N_1 = N^* > N_2$. Therefore with strategy 2 there is unemployment:

$$U = N^* - N_2$$

2. The necessary conditions to prefer the more productive strategy.

In order to have a higher output with strategy 2, in such a way that the statement [1] could hold, to have a higher productivity associated with such strategy is not sufficient. The positive productivity differential must be large enough to compensate for the fact that less people are actually working; in other words this differential must be somehow proportional to the level of unemployment which is associated with the most productive strategy.

Very simple algebraic elaboration of [1] allows to state such proportionality condition: 'in order that the most productive strategy 2 can produce a higher output, the productivity associated with it must exceed the productivity associated with the less productive strategy 1 by a proportion equal to the ratio between the unemployment and the employment associated with the most productive strategy 2' (see appendix 1). Which simply means that, if the ratio between those who are employed and the unemployed ones produced by strategy 2 is, for example, 10%, the average productivity associated with the most productive strategy 2 should exceed that associated with the less productive strategy 1 by at least 10%.

As we said earlier, European governments 'chose', around the mid of the 70's, type 2 strategies. As a consequence, labour productivity began to grow very rapidly, almost twice as fast than, e.g., in USA, and unemployment began to grow as well. We are bound to suppose that, when each government did that 'choice', it estimated that the proportionality condition for preferring the most productive strategy held. And perhaps governments were right at the beginning. But how could we be sure that the preferability condition continues to hold true? We simply cannot.

What suggests, anyway, that a negative answer to the above question is more likely to be true than a positive one is the observation that not only the level, but also the rate, of unemployment, kept growing.

As a matter of fact, the purely descriptive (and basically tautological) 'model' presented above is too simple to allow to deal with the fundamentally dynamic and anyway complex problems which are posed by the choice of strategies which put our countries along a competitive 'path', and therefore many further considerations should be developed; but the model has the advantage of being very clear, and therefore we will continue to use it, at least for the moment.

3. Mixed strategy: Options and difficulties.

Let us suppose that the proportionality condition stated above as being sufficient to prefer the most productive strategy 2 holds, and that strategy 2 is feasible. Any wise, imaginative, and non-economist reader would be likely to suggest a third strategy (strategy 3), conceived as a combination of the previously considered ones. In fact we could employ N_2 workers at an average productivity v_2 -as it is possible with strategy 2- and then employ, although at the lower average productivity v_1 , those who are left unemployed, U . In this case we would have in fact

$$Q_3 = v_2 N_2 + v_1 U > Q_2 = v_2 N_2 \quad [2]$$

Better than that, we can state an even more general proposition: 'it is always convenient, from the point of view of output maximization, to employ an unemployed worker, at the only condition that his productivity is non-negative'. In fact

$$Q_3 = v_2 N_2 + v U > Q_2 = v_2 N_2 \quad \text{for any } v > 0 \quad [3]$$

In fact strategy 3 is the one which would be selected -and is actually adopted- in any non-market system (or sub-system), provided only that there exists a set of social rules for a proper allocation of people among jobs and for a commonly accepted way to divide the system's output among the people who contribute to its production. This is what happens in any administrative institution, in any family, in any rural environment, in any community household; in brief, in any social aggregation in which a direct attribution of tasks is possible.

This objection can be resisted, though containing some, and unfortunately quite persuasive, elements of truth. We will delay to section 5 a full development of this issue, except for one single point, dealt with in the remaining part of this section.

The implicit assumption behind the above mentioned objection is that the whole output is produced under strict market conditions. It would not apply, therefore, under a different regulatory regime that could allow a suitable mix of different allocative and regulatory mechanisms.

This is not to deny the theoretical and technical difficulties, not to mention the political ones, that would hinder the invention of such a regime, but simply to stress the essentially regulatory nature of the problem, and to argue that a solution exists, as the basic wisdom of formula [3] above clearly shows.

As a matter of fact, formula [3] is nothing else than the rationale of a part of the presently attempted job creation strategies. As it is well known, such strategies are not only meeting heavy practical difficulties in their implementation

and severe political opposition, but they are often criticized on the basis that they lack economically rational foundations.

This is not true, and not only on the basis of the argument of formula [3], but also on the basis of a more correct use of the analytical tools provided by the most established tradition of political economy, as we will convincingly show in the next section.

At the end of this chapter we will attempt to establish a strict relationship among this argument and the criteria for the evaluation of public projects implying additional employment; and, on such a basis, we will provide a critical revision of traditional cost/benefit analyses, which will result useful up to the point of possibly playing a strategic role in the set of proposals we will develop, in the next chapter, in order to face, at the European level, the problem of unemployment or, rather, the problem of how to organize our societies in such a way as to avoid the enormous and irrational waste of resources which presently affects them. But before doing this, we have still to deepen the competitiveness argument.

4. Technical versus labour cost competition.

In the previous section, we might have given the impression that competitiveness depends only upon technological efficiency. This impression is false. We choose to argue in terms of productivity because of two different reasons. The first one was the need to give the reader the substance of the argument in a compact way, without confusing him with an excess of issues in an early stage of the analytical development.

The second reason was that we were interested in showing, since the beginning, that the system's performance always improves as its employment level grows, at the only condition that the additional workers have a positive productivity. And we consider this point as being very crucial, since it is the obliteration of this simple and perfectly common sense truth which has made persuasive the opposite message: that is, that a strategy which associates more unemployment with a higher productivity is the best one to adopt. And it was an excess of complication, embodied precociously into the analysis, that has allowed the concealing of the obvious truth stated above. Time has come, now, also for us, to complete the analytical set-up.

Commodities compete in terms of their market price, which depends not only on physical productivity but also on input prices, and, in particular, on wages. Suppose that labour is the only input; as we saw earlier total output will then be $Q = v N$, the total cost of which will be $C = w N$. Therefore, the unit cost, c , will be

$$c = C / Q = w N / v N = w / v \quad [4]$$

that is, the unit cost is positively related to wages and negatively to the productivity. It will be lower the lower is the wage rate and the higher is the productivity.

Since the price will anyway be some function of unit cost (it will be, in fact such cost, plus a margin over it), this implies that one can improve his competitiveness either increasing productivity, v , or lowering the wage rate, w .

The competitive game between firms (or between sub-systems) can thus be started either because some of them succeed in increasing their productivity, or because some of them succeed in cutting the money wages paid to their employees.

It is not very important to establish who (which firms, which sub-systems, which countries) began the competitive game sometime in the mid Seventies, nor it is important to establish how -whether in terms of productivity increases or in terms of wage cuts. What matters is that, once the game had been started, both strategies were used and wage cuts are not likely to have played a secondary role, with relevant social, as well as economic, negative feed-backs.

5. A further development of the competitiveness argument.

Let us go back now to the competitiveness argument, and in particular to the possible objection that we left partly unanswered in section 3. The objection was that the suggested combination of strategies 2 (the more productive one) and 1 (the less productive one) is not possible, once society has chosen to adopt a market allocation mechanism; once this has been done, the market forces themselves would squeeze out the less competitive strategy. Therefore either we 'have' strategy 2 or we 'have' strategy 1. We cannot 'have' both of them at the same time, unless for a short and transitory period, during which strategy 2, once available, is squeezing out strategy 1.

The point can be summarized in the following way. Under market conditions, the products compete regardless of the techniques with which they have been produced; therefore, if one better 'technique' happens to become available (the one associated with strategy 2) and adopted by some of the competitors, the output produced with that technique costs less and can be sold at a lower price. The commodities produced with the inferior technique cannot stand such price competition, unless the firms adopting such technique are subsidized -but this would violate the rules of 'fair competition'- or unless their workers accept to lower their wages in a proportion that could match the productivity differential of the competing techniques. Even in this latter case, however, in the long run the competition in the labour market would restore labour costs homogeneity, and the best technique will definitely squeeze out the inferior one.

We will try to demonstrate here that this argument is not only insufficiently specified, but that it cannot stand any relevant test of 'realism', in the light of how modern systems of production and labour and labour market relations actually work in industrialized societies. But before doing so, notice that the argument does not say anything, in itself, about whether the system will have or not full employment. The reasoning, in other words, applies only to the 'transition' among differently productive (or 'efficient') techniques. Whether there will be full employment depends on other things, which are not directly considered by the argument, but that we have already recalled in the previous chapter, and treated at length in our 1986 Report: that is, it will depend -at least within a system 'closed' to international competition- on whether money wages are set in the 'right' proportion with the average price of commodities, 'given' the productivity. Therefore we could have -according to this argument- or have not, full employment with both strategy 1 and strategy 2. The above perspective, that is substantially shared by both neo-monetarist and neo-Keynesian schools of thought, strictly depends on the hypothesis of decreasing returns to scale, which implies a model which makes the scale of the system depend only on real wages: the higher is the average level of commodity prices with respect to the average level of money wages, the higher would be the output and the employment.

Considering the effects of the introduction of a more efficient technique, we said that the two techniques could coexist in so far as the workers employed with the inferior technique accepted a wage cut proportional to the productivity differential among the competing techniques. More precisely, it can be said that the two, differently productive techniques can coexist if between differently productive firms (or sectors) there exist proportional average wage differentials; which is an event the occurrence of which is far from being unlikely in the real world. Notice in fact, for example, that the choice among the techniques would be balanced also in the case that the workers employed with the better technique had obtained a proportional increase in their pays: what matters, in fact, is that, if we call $w(i)$ the wage of the workers employed with technique i (with i indicating technique 1, technique 2, technique 3, etc), and $v(i)$ the productivity of a worker employed with technique i , the following condition could hold:

$$c = w(i) / v(i) = x^* \quad [5]$$

where x^* is a constant equal for each of the techniques i , and this result can be ensured by any combination of higher wages for the workers associated with better techniques and lower wages for the workers associated with worse techniques.

What the above considerations make clear is that the thesis that differently productive techniques can not coexist strictly depends on the hypothesis that one of the following assumptions hold:

(a) wages paid for equal jobs are strictly equal and depend only on the subjective skills of every single, potentially highly mobile, worker;

(b) wages paid by differently productive firms can be either equal or different, but that, once established, they are rigid, that is, they are not subject to change if the productivity differential between firms changes, as the consequence of the adoption, by some of them, of more productive techniques.

In both cases the structure of wages has to be rigid, although in association with two completely different underlying mechanisms. But in order to better understand this point an important preliminary remark has to be made: The term 'productivity' referred to workers is very ambiguous indeed, and can have two distinct and very different meanings. The different productivities $v(i)$ used in formula [5] above do not depend -in the above considerations- on the subjective differences among the workers, but on the fact that the workers are employed with differently efficient techniques. Let us call these differentials in productivity 'objective productivity differentials', in order to distinguish them from those which eventually depend on subjectively different personal endowments, which are exactly those to which traditional marginalist analysis uniquely refers.

As we saw, the competition between differently efficient techniques requires, in order to be possible, that wages have to be relatively rigid, so that they do not adapt, rapidly and in a smooth way, to the substitution of techniques.

This result -we said- can be obtained through two very different mechanisms. The first is a very high labour mobility (based on both dismissals and voluntary quits). This would in fact produce an equilibrium allocation of workers among jobs which would depend only upon 'subjective productivity differentials', with each worker receiving a relative wage which is proportional to his 'subjective' relative productivity. Once obtained, this structure of job allocations and pay conditions would remain stable (as long as the same mobility conditions continue to allow for the necessary adjustments) and, thus, relatively 'rigid' from the viewpoint of the adjustments of pays eventually related to 'objective productivity differential'.

The second mechanism is a 'regulated' wage structure, that is, by a situation in which wages are determined according to a set of economic, institutional and social rules, created and changed in a complex sequence of historical paths and as a consequence of complex and time consuming interactions among several agents (besides the firms themselves and the involved workers, the employers' and the workers' unions, the governments and the parliaments, the courts, the educational and training institutions, and so forth). Useless to add that, from a historical point of view, it has been this second mechanism which has largely prevailed.

This change of perspective, however, has further relevant implications for our 'transition' problem, both within a case of 'infra-system' competitiveness and within a case of 'inter-system' competitiveness. Such implications will be developed in the next section.

6. Positive and negative sum games.

The basic rationale of standard economic theory is that the game of competition is one which maximizes the prizes which are available for the whole of the participating gamblers. In other words, the game allows the gamblers to produce (as a part of the activities of which the game itself consists); if the gamblers adopt a competitive strategy, the resulting total production will be larger than the production that would result as a consequence of the adoption of alternative strategies (as, for example, cooperative strategies).

Present as well as past history tends to demonstrate the opposite. Full employment is in fact rather the exception than the rule; furthermore, high levels of employment have been attained only under regulatory frameworks which controlled and integrated purely market forces. More in general, the forces of cooperation and social solidarity have contributed to the structuring and the development of our economies and of our societies -as they presently are- certainly not less than the purely antagonistic forces which dominate market interactions.

This is not to deny that the market is a rather powerful allocative and regulatory mechanism; just to acknowledge that is one among others, and that it is usually not sufficient to ensure an acceptable performance of our economies. Furthermore, not always do real markets reproduce some of the essential features of the highly stylized abstract markets that the economists use and upon which they derive their statements about systemic optimality. The considerations about the wage structures and their possible changes single out one of such possible inconsistencies, which happens to be extremely relevant for our analysis.

The reasons why we prefer to use these factual arguments is that they should be convincing enough here, while we could not pretend to survey or not even to summarize the whole of purely theoretical arguments which have been raised against the theories which hold the optimality and self-sufficiency of market allocation. We shall limit ourselves to very few and very specific arguments, connected -as anticipated- to the 'transition' argument explored above in section 5.

Suppose that each 'firm', or sub-system, $S(j)$ (so that $S(1)$ is 'firm' 1, $S(2)$ is 'firm' 2, etc., as $j = 1, 2, \dots$) has a share $Q(j)$ of the total market (of the whole system) Q which depends on the ratio between the price of its output $p(j)$ and the average level of prices, p^* : the lower is such a relative

price, the larger is its market share, as it is shown -for example- in the following prospect:

$p(j)/p^*$:	1.00	0.95	0.90	0.85	0.80
increase in market share:	0.00	0.05	0.11	0.18	0.30

Suppose, furthermore, that such a price results from the application of a fixed coefficient $m > 1$ to the unit cost, so that

$$p(j) = m c(j) = m [w(j) / v(j)] \quad [6]$$

Any firm (or sub-system) can start the competitive game, either improving its productivity or succeeding in changing the rules which determine the wages. Suppose, for example, that a firm is able to decrease its prices by 0.05 at each 'round' of the game, aiming at lowering its relative price down to the level of 0.80 within the fourth round, so that it could increase its market share by 30%, as it is shown in the prospect above.

It is obvious that the gamble can not succeed if the other players adopt, in reaction, a similar strategy; in fact, in so far as each of the players will succeed in cutting their prices, the average level of price will decrease, and thus tend to restore the previous levels of relative prices. Any gain in the market shares is thus bound to be transitory. Nevertheless, if each round of the game is long enough, and if the players are not conscious of their reciprocal interdependence, these transitory gains will be sufficient to make the game last.

We have, thus far, a basically zero-sum game, which, once put into motion, tends to last. This result, however, strictly depends on the fact that we did not consider the systemic effects of the changes affecting, because of the game, wages, productivities, and possibly the overall levels of demand and productive capacity.

Once we take them into consideration, the game is likely to manifest itself as being a negative-sum one. This is basically due to two different causes, the first one dealing with aggregate demand, the second dealing with employment levels and labour standards. Obviously, when we talk of a negative sum game we refer to the whole system and not necessarily to each of the involved parties; that is, referring to the European arena, we say that the whole of the EEC 'system' is bound to be worse off, while not denying that some of the EEC countries could find himself being better off. 'Better off', however, with respect to what? With respect to other countries certainly yes; with respect to a completely alternative game is instead rather doubtful.

The 'game trap' stays, indeed, in this bias of perspectives. The first possible bias is given by the fact

that players fail to understand that they are playing a game, and in particular a negative sum game; that is, they are not conscious of the interdependency among their strategies, and therefore they do not understand that the ineffectiveness of their strategies is due to such interdependency and not to the features of a perverse 'state of nature'.

The only thing they perceive, while unconsciously playing the game, is that if they succeed in being more competitive - and as long as they keep succeeding - they are better off than they would be if they stopped to practice the search for competitiveness. And this perception is the first of the factors that make the game continue, as it is difficult to shift to a different game.

The second possible bias is given by the fact that none of the players is conscious of the situation in which he will find himself, should a completely different game exist. And this is the second factor which, hiding the very same option of changing the game, forestalls a major change of the rules.

7. Systemic negative feed-backs.

For any given time-rate of increase in productivity, either the time-rate of increase in demand and output is at least as large, or the level of employment is bound to fall. This is exactly what happened in the EEC countries in the last decade or so.

On this issue we have different schools of thought. According to those who totally believe in the self-regulatory mechanisms of market forces, the real wage rates are still exceedingly high; should they lower more than they actually did, the activity rate of the system would increase, up to full employment. Historical experience seems to militate against them; unemployment has kept growing in the last decade or so, while real wage rates have kept decreasing or, at least, remained stable.

A slightly different view says that the overall demand can be kept under the control of policy makers; but they could not, however, allow the demand to increase at the same rate of productivity, because if they did, the system would have faced unsustainable pressures from the point of view of both inflation and external imbalances.

According to us, the two constraints mentioned above cannot be considered as being similar. The external balance constraint depends on the international competitiveness game; more exactly it is a part of it (that is why we talked of 'strategies' since section 2 above). If this is true, it can be released or softened only through more international coordination and cooperation; a form of coordination and cooperation that could interrupt, or at least regulate, the international negative-sum game.

As far as inflation is concerned, we have to recognize that the argument is very serious, and that economic theory has not been able, until now, to deal with the issue in a way that could result at the same time satisfactory and widely accepted.

In sections 2.7 and 2.8 of our 1986 Report we attempted to develop a suitable dynamic explanation of the sources of inflation. Such explanation had the advantage of giving a consistent account of several contextual phenomena which appear to have -or have had- a role in determining the present scenario: not only the inflation but also the search for flexibility, the reduction of employment, and the reduction of productive capacity (what the experts of CEPS correctly stress, calling it 'capital decumulation', failing, however, to give a consistent explanation for it).

We can summarize it here (but we will develop it further in the course of next chapter) by saying that the set of strategies previously outlined, together with their systemic effects, are perceived by firms as signals against the likelihood of a widespread recovery. Such negative expectations will lead firms to concentrate their investments on productivity gains, without widening their productive capacity (unless indicated by the prospects for expansion of specific commodity markets which do not depend on the possibility of a generalized recovery). This makes for a rigidity towards expansion of aggregate supply, and makes the systems more vulnerable to inflationary pressures.

In the meantime countries continue to compete each against the others. However, since the possibility of increasing productivity is limited, the competition increasingly affects wages and labour standards, which constitute, under certain circumstances, the only 'free' variable left, as we will argue in the next section.

8. Labour standards and competition.

Within and across socio-economic systems, an equilibrium could establish itself that allows for a certain level and structure of labour and social standards, which on the one hand guarantee relatively fair, or at least acceptable, working conditions, protection against arbitrary lay-offs, social security benefits, etc., and, on the other hand, contribute to maintain a relatively good standard of living, a relatively acceptable distribution of income, wealth and jobs, good standards for the reproduction of the labour force and of human resources in general, and a suitable market for growing production.

Such an equilibrium existed around the sixties, and had been built up along the previous decades; many scholars regard this as the source of the second post-war affluence.

'Equilibrium' is intended here in a rough sense, and does not imply that labour and social standards are equal, and not

even homogeneous, across competing systems (regional, sectorial, national). It simply implies that the repercussions that the standards have upon the relative competitiveness of systems are such as not to produce major imbalances in the exchanges of commodities that take place among them.

Within each system the standards can be maintained so long as strongly shared -or imposed- social or legal common rules are respected, and so long as free-riding is repressed. This implies, in other words, that production costs include a share of what we can call 'solidarity costs' -or 'solidarity bill'- that is accepted and does not alter competitive equilibria so long as all of the competitive agents bear them more or less homogeneously.

This kind of equilibrium among countries is obviously much more fragile, and it is more easily kept when the levels of international trades are relatively minor and as long as trade balances are effectively regulated through appropriate coordination instruments. However, the possible help of common social and cultural concerns, or more in general of social and political values, should not be overlooked.

The lowering of the 'solidarity bill' is rewarding for each of the involved systems (or agents within the same system), since those which succeed in doing it first could gain in relative competitiveness. Moreover, given an initial disequilibrium, its meaning tends to be magnified as the inter-exchange among systems grows, reinforcing thus the pressures to shift to aggressive behavioural patterns, based upon the undercutting of the solidarity bill they bear. Notice that, once this competition has begun, the other systems (or agents) have no other choice than following the same patterns, and therefore retaliating.

This is what appears to have happened since the Seventies at the international level. In fact the most industrialized countries moved along a path of progressive deregulation of their labour markets, dismantling their welfare systems and labour standards.

This game, which was begun by governments, which believed they could contribute in this way to keep under control inflation as well as external imbalances, and by employers, who had evident vested interests in doing so, ended up in involving even trade unions, so powerful is the strength of cultural stereotypes (see our 1985 Report).

The nature of negative-sum game of such patterns of interactions is obvious, as we noticed before, once one puts himself in a systemic perspective. The perception of this, however, is unfortunately not sufficient to revert the presently prevailing attitudes, given the apparent certainty of the immediate gains earned through the continuation of selfish adjustments, the convenience of free-riding, the unlikelihood and the difficulty of reaching cooperative solutions, and finally given, the lack of immediate political

rewards associated with the construction of a proper negotiation set-up.

9. A critical appraisal of standard cost/benefit analysis.

As anticipated, we will attempt, in the remaining sections of this chapter, to reconcile the macroeconomic reasoning of sections 1-4 with the problem of the criteria for evaluating public actions involving additional employment.

Can we accept, without further qualifications, the proportionality condition we stated in section 3 above as being 'sufficient' for preferring the most productive strategy 2? In order to say that a situation is better than another one, is it really sufficient that the level of output is larger? Would we really be ready to accept any rate of unemployment in order to have more output?

No policy maker -we believe- would dare to provide a straightforward positive answer to the above questions. Though, the very same policy maker would be likely to refuse a job creation project, the benefit/cost ratio of which is, for example, 0.99. But how the costs and benefits are computed, even according to our best cost-benefit ordinary techniques?

Here is the answer, stated in the simplest possible language. Suppose we have a project that requires - in order to produce a given result B- to buy certain inputs I on the market, at a price $p(I)$, to hire a number of well trained engineers N_1 , at the wage of w_1 , and a number N_2 of unskilled workers, at the wage of w_2 . Suppose furthermore, for the sake of simplicity, that engineers are fully employed, while unskilled workers face a very high rate of unemployment, and that, for some constraint, the present production of I cannot be increased, so that, in order to sell it to the project, it fails to be sold elsewhere. The financial cost of the project will thus be

$$FC = p(I) I + w_1 N_1 + w_2 N_2 \quad [7]$$

The real cost, however, would in this case be different, since the unskilled workers are unemployed. Thus, while the hiring of engineers will determine a loss of production in the system (since, being fully employed, they are withdrawn from some other jobs and they can no longer produce what they produced in such jobs), and while the inputs I have a meaning in terms of real costs (since they can no longer be used as they were previously), the hiring of unskilled workers does not imply any loss in production, since (and in so far as) they were not producing anything. (This is true only if unemployed do not really produce anything. If there exists a 'disguised' production, there is also a loss in unofficial production. It may be very difficult to estimate such a loss, but the point is relevant also for the effects on the supply of labour.)

Real costs, in fact, consist in the production which is foregone and in the uses of resources that are displaced because of the adoption of the project; since no production is lost as a consequence of employing the unskilled workers, this implies that the real value of their work is zero, despite the fact that they are paid a money wage w_2 ; the 'true' value of their work is -according to standard cost/benefit analysis- a 'shadow price' (in this case a 'shadow wage'), $w^* < w_2$, which corresponds to the value of foregone production, if any (in this example, as we said, is zero, but it could also be a positive value -although smaller than the prevailing wage- if some production is foregone or some use of resources is displaced because of the hiring of the unemployed people). The real cost will thus be

$$RC = p(I) I + w_1 N_1 + w^* N_2 < FC \quad [8]$$

The project will be adopted if what is produced, B , is larger than or equal to its real cost RC , independently of the purely financial cost. Therefore, in this case, the 'standard of value' is the real value of the product. This 'rule' perfectly corresponds to the 'sufficient' proportionality condition illustrated in section 3 above.

However it is also evident that no positive value whatsoever is attached to lowering unemployment, despite what policy makers might officially state in an opposite direction, when they are directly questioned about unemployment; at least as long as the above described way of performing cost/benefit analyses will continue to be adopted.

If a positive value were actually attached to lowering unemployment, this should result in the feasibility (that is, acceptance) of projects for which $RC > B$ (computed as in formula [8]), at the condition that the elimination of that unemployment is estimated to have at least the same value of the loss of production ($RC - B$) associated with the adoption of the project.

In fact, saying that something (unemployment) 'has a value', implies that one is ready to give up something else (production) in order to get some more of the former. This is not new. If one has several partially incompatible goals, so that one can not reach them all, one has to 'trade off' (as economists say), or to 'sacrifice' (as ordinary people say), some of the goals in order to obtain more of the remaining ones.

Nothing new, as we said. Do you remember the Phillips curve regarded as 'a menu of economic policies'? Since less unemployment appeared to produce higher inflation rates, the policy maker had to choose between some point less of the rate of unemployment and some point more of the rate of inflation; and the actual choice depended -it was said- on the relative importance that the policy maker attributed to lowering unemployment in relation with the stability of prices.

It is of no importance, here, whether the above described perspective was right or wrong. It was widely shared among both, economic experts and policy makers. And since most of the countries, then, accepted to have some inflation, this implies that policy makers attached -then- some positive value to the reduction of unemployment; 'then' -notice- when the unemployment rate was much lower than now. Why should it have no value at all today?

10. Productive and unproductive labour: Some suggestions from the classical scheme

The point is, in our opinion, that we are presently strongly biased, from a cultural point of view, by an unsound system of values which pivots around a distorted way of looking at market efficiency and the competitive aggressiveness we have dealt with in the course of this chapter.

The current situation, from the perspective of the labour-force structure and composition; can be better interpreted if we adopt - though in a critical way - some analytical suggestions originally developed by classical economists. We refer, in particular, to the concepts of productive and unproductive labour.

Let us start by expounding, very briefly, what Classical economists (Smith, Ricardo, but also Marx) intended by 'productive labour'. In brief, labour is productive if it is employed by capital and, in the process of being employed, gives rise to a profit, i.e. a monetary surplus, a value exceeding that which has been advanced by the capitalist entrepreneurs to hire labour itself and to buy raw materials, machines, etc. On the contrary, all labour that does not produce a profit for its employers has to be regarded as 'unproductive' (namely, unproductive of a profit).

In these definitions, the qualitative attributes of the produced goods (and/or services) do not play any role. Workers producing the same goods can be productive or unproductive. If they work under capitalist rules they are productive.

From this point of view, for classical economists, all workers which are employed by the state are unproductive. Although they produce useful and indispensable goods and services, they do not produce a profit since the state is not concerned with obtaining a profit but only with ensuring an orderly functioning social system and with providing those infrastructures which allow the society as a whole to reproduce and grow. Unproductive labour is useful (it produces use-values) but is not employed in view of obtaining a profit.

Classical economists, however, realized that some qualifications were required. They introduced, though not explicitly, a third kind of labour which we may call 'indirectly productive' labour. Indirectly productive workers

are those whose produce (goods or services) contributes to raise the rate of profit in the capitalist (market) sector. They do so by lowering costs of production for firms. Obvious examples are to be found in all those cases of state workers which are employed to produce goods and services which enter into the productive processes of capitalist firms: building roads, bridges, railways, etc. In all these cases, the state takes care of production (because no private firms would start such productions in that they are not regarded as profitable), and then provides those goods and services either free or at a price which is below their 'natural price' (that is, the price that would ensure a normal rate of profit for the supplier). Thus the capitalist sector is enabled to acquire some of the required means of production at a price which is below that which would prevail if those means of production had been supplied by the capitalist sector itself. Costs of production are lower and hence, the rate of profit is higher.

In order that the state play this role it is of course necessary that the goods and services produced by it are of a kind that are used, directly or indirectly, in other productive processes. By using modern terminology we can define indirectly productive workers in a more precise way. They produce basic commodities which are made available by the state at a price which is not inclusive of a profit. Indirectly productive workers do not produce any monetary surplus for their employer but allow the capitalist sector (and, hence, workers employed in it) to give rise to higher returns.

So far, in spite of some simplifications and without paying attention to differences among classical economists, we used concepts and ideas which have been present in economic thought for almost two centuries. Let us now see, whether those concepts can be useful to our current purposes.

Modern market economies are characterized by such a pervasive state intervention in the economic field that the classical concept of indirectly productive labour appears quite useful, indeed more significant than it might have been when classical economists wrote. In fact, in a way or another, this concept has been recently used and referred to in the debate on the economic role played by the state in Western economies.

But there is another aspect which deserves attention and leads us to some aspects that appear significant in our current context. If the category of indirectly productive applies to all those workers who produce means of production, why should it not apply to those workers who play a role in the process of production and reproduction of the labour-force itself (eg. education, health care, etc.)? Public intervention in these sectors lowers the cost of production/reproduction of the labour force for the capitalist sector. It provides workers whose productivity is higher without making the private sector pay for such a 'higher quality' output. Thus, also workers employed in these areas of the public sector have to be regarded as indirectly productive. From this

perspective, the economic meaning and relevance of state intervention acquire new dimensions. It is easier to appreciate the importance which state intervention has - and, presumably, has always had - in market economies.

However, widening the original classical concept of productive labour along the lines suggested above raises some methodological issues. If we agree to define as indirectly productive all those workers who not only produce basic means of production in the public sector but who also 'produce' labour-force, why should we not consider as indirectly productive all those workers who, outside the public sector, play a role in the production and reproduction of the labour force, even though they do not give rise to profits for their employers? The example of women who perform unpaid domestic services is the most immediate and obvious. They certainly take part in the process of production and reproduction of the working force (their husbands, children, etc.) but they do not produce profits and, indeed, are not even included in the official working force.

Once we adopt such an approach to the definition of labour, however, the original simplicity and clarity of the classical definition are partly lost, so that one wonders whether it is still worth while to use it. The simple and straightforward rule to establish the 'productivity' of workers does not exist any longer, and for every kind of occupation, one has to investigate whether its output affects the conditions of production and reproduction at the systemic level. This is not an easy task to perform. But we are not saying that it should be done 'across the board', in any possible case; but what we certainly imply is that we should be very careful and have a more inquisitive attitude whenever the real productivity of actions (both public and private) is superficially challenged.

We may conclude by saying that, although the distinction between productive and reproductive labour is no longer as relevant as it might have been in the classical period, the public sector intervention certainly does not merely represent a waste of resources. Resources (workers) which are 'subtracted' from the market sector are not merely devoted to unproductive (wasteful) uses but they might be highly productive from a global systemic point of view. A fortiori this statement should in general apply to workers which, under normal circumstances, are kept unemployed, that is, idle.

If we apply this approach to the issue of public employment, job creation through public spending immediately takes on a different meaning. Public job creation would not be simply a 'cooperative' diversion of resources (from the private to the public sector) to alleviate social problems and tensions. It would also be a form of 'social investment': those resources publicly employed would determine an overall higher productivity at the aggregate level.

But if this approach, on the one hand allows us to look at state intervention from a more general -and a more correct- perspective, it, on the other hand, also implies greater responsibility for the public sector itself. What we said about public employees does not mean, in fact, that any form of public employment is 'indirectly productive'. On the contrary, in many areas, public employment may represent a mere waste of resources, in that the output does not affect the aggregate national output in any positive way. In these cases public job creation is likely to be an inefficient form of income redistribution. Therefore, labour policies aiming directly to create jobs must be very careful in the choice of the areas and of the outputs to be provided through the newly created jobs.

There is a last issue which has to be dealt with. Public goods and services which are 'functional' to production and reproduction at the global level also affect the living standards of the recipients in a very evident and clear way. In the case of the working classes, in particular, it is a form of demand for higher wages/services. Therefore it is not at all surprising that the demand for these public goods and services has grown fast.

But here we have the same contradictory aspects that we can see in the roles played by wages paid by the market sector. On the one hand, wages are 'functional' to the process of reproduction in that they allow the labour-force to reproduce itself and to ensure this fundamental means of production; on the other hand, wages -and, in particular, wages increasing too fast- imply negative effects on the economic system as a whole, to the extent that they jeopardize profits and the profitability of producing and investing.

Some of the services provided by the public sector enter into the consumption of the labour-force and, hence, the demand for them cannot be regulated only by the needs of the process of reproduction. On the contrary, the demand for them is also regulated by the labour-force's attempts to raise and improve its living standards (in the same way as an increase in monetary market wages does). If this second factor underlying the increase in the demand for public goods/services prevails, the effects on the process of growth at the systemic level can be negative, even though the global social effects (a better social system) can be largely positive.

We might interpret the recent confrontation over dismantling the Welfare state in many Western countries from this perspective. Many feel that the current situation is characterized by unacceptable distortions in the basket of goods provided by the public sector: there are too many services and goods which, though useful to the labour-force, are 'unproductive' for the economic system.

CHAPTER IV

CHANGING THE GAME TO CREATE A NEW ENVIRONMENT

1. The elements for devising a strategy...

In the previous chapters we have accumulated a wide and articulated set of elements which can be utilized in order to frame and to build up a complex strategy, or, rather, a set of coordinated strategies suitable to attempt a way out from the present crisis. We find it useful to summarize them here.

1. There is a set of negative interdependencies, acting at the international level, which produces, and contributes to maintain, a negative sum game. The main features of such a situation are the following ones.

1.1. Various economies (and among them, in particular, EEC countries) have become heavily integrated, up to the point of having substantially generated a real new system. Such a system, instead of having a unique decisionmaker and regulatory agency, as it would be appropriate for any system, is actually ruled by many governments, which act in an uncoordinated and conflicting way.

1.2. The economic systems, which formerly competed only at the level of international trade, increasingly compete at the level of economic policies.

1.3. It is difficult to abandon the present game. While the continuation of aggressive and competitive strategies promises some, although transitory, advantages, the behaviours which are needed to abandon the game appear to generate possible losses, which are higher the larger is the risk that other countries keep on playing the old game. Furthermore, the perception of the advantages possibly deriving from a new game requires a good deal of imagination, trust, and intelligence.

1.4. The aggressive attitudes which have been developed at the international level reverberated at the level of domestic national arenas, eroding the attitudes favourable to cooperative strategies, both at the national and international levels.

1.5. In each of the involved countries there are pressures in favour of autarkic strategies.

2. Domestic macro-policies conjure with the above described international situation to create an extremely turbulent, negative and uncertain framework for firms' expectations.

2.1. This climate produces negative attitudes, on the side of the firms, towards expanding their productive capacity (their capital as well as their labour 'stock'). Such attitudes are perfectly rational, since the framework described above is far from suggesting the likelihood of an enduring expansion and of the fact that policy authorities would not interrupt expansive spells.

2.2. Inflationary responses to expansive spells are generated either by a dynamic shortage of supply, due to lack of productive capacity, or to the fact that firms, given such a context, anticipate the events by 'betting' on price increases.

3. This systemic 'disease' was initially generated by a series of changes occurred in the international arena and in macroeconomic policies. Further causes and associated events, however, enter into the picture, contributing to structure the overall final result.

3.1. There has been a deterioration of industrial relations, due to a sharper conflict upon wages and a more intensive search for flexibility on the side of firms. There is now a major uncertainty about the most appropriate strategies for personnel management.

3.2. There has been an acceleration of organizational and technological changes.

3.3. There has been a deterioration of the technological environment.

3.4. There has been a deterioration of the qualitative trends concerning policies about human resources. The progressive educational and social policies envisaged between the end of the sixties and the early seventies failed to be maintained and/or implemented; their formal structure, when maintained, was gradually filled by different aims and contents. The efforts towards the promotion of general and higher education were substituted by narrowly conceived training policies.

3.5. There has been a loss of control upon the trends of public expenditure, while its quality deteriorated and/or the public interventions became less effective. The image of the public sector among ordinary people deteriorated as well.

4. We know that production would be larger if we succeeded in making it possible for the unemployed to work, only provided that their productivity is positive, though smaller than the 'normal' productivity in the sphere of marketable goods (see the last two sections of chapter 3 above). Such production might increase the level of well being of the population, or result in a higher productivity of the system, or both, independently of the fact that such positive results are acknowledged or not in terms of market values.

5. We know that plain expansive Keynesian policies would be, in the present environment, quite ineffective. They would result in a higher degree of inflation and would not induce any increase in the level of productive capacity; this would be the contrary of what we should aim at. The only way to obtain the widening of productive capacity is to convince firms that there will be an increase 'in the things' that will be demanded, that there will be such an increase regardless of whether they will raise their prices and that it is bound to last. The only way to avoid a higher rate of inflation is to keep the expansion of demand at the same pace as that of productive capacity, while finding a way of discouraging bets upon prices.

2. ...and their broad implications

The main policy implications are the following ones:

(1) Labour policies, and in particular the youth unemployment policies which have been widely adopted by EEC countries, are fundamentally useless, since none of them is appropriate to deal with the set of problems which have been - in itself and within the present context - outlined. Some of the labour policies could result useful, but only within the framework of an entirely different setup.

(2) No policy, if undertaken by a single country without coordination with the other connected ones, could obtain any relevant result. The main difficulty, however, is to push countries to collaboration and coordination. Because of this, it is better to avoid attempts to get very wide agreements among countries, and to search for effective agreements among a limited number of countries, at least at the beginning. The ideal target would be to reach suitable agreements among EEC countries; but even a more limited coalition could constitute a good starting point.

(3) The most important target is to establish a climate of credibility about the undertaken policy arrangements. This, in turn, implies

(1) that the agreed structure of international coordination be credible; in order to have this, the behaviour of most countries should obey to clear automatic rules, that should be established through

national laws before implementing the discretionary parts of macro-expansive policies;

(ii) that the pursued expansion should be moderate and gradual;

(iii) that the pursued expansion should be announced mostly in real terms, that is, it should be openly translated in terms of programmes about 'things to be done'.

(4) Macro-policies should be supported and integrated by consistent micro policies, fostering the effects of the former upon the needed increase in productive capacity, while discouraging bets on prices and rewarding firms that choose to expand real output and employment. The structural design of such, entirely new, micro-policies will be actually described in section 6 below.

(5) The fifth implication is that the policy of coordination and cooperation at the international level should be replicated within the single countries. A new launch of cooperative strategies and of cooperation among otherwise conflicting parties would contribute

(i) to stabilize positive expectations, reinforcing the framework of certainties;

(ii) to corroborate the credibility of the adopted macro-policies;

(iii) to corroborate the climate of international cooperation.

This implies a strict collaboration/negotiation between planning authorities and social partners, to set the likely and/or desired values of the main macroeconomic magnitudes, to stipulate the set of consistent behaviours to which the negotiating partners have to comply, and to define the sanctions for failure and the rewards for success (the past Austrian experience is very suggestive in this respect)

(6) Macro policies should be integrated by additional policies, aimed at forestalling the idleness, and thus the deterioration, of labour and human resources in general, through special job-creation programmes. The feasibility criteria for the choice of such programmes should be agreed internationally, along the lines suggested in the previous chapter of this Report. For each individual there should be the guarantee that it will not be allowed that he remains idle for longer than a predetermined and clearly defined length of time; incidentally, this would contribute in itself to keep a favourable climate of expectations, since firms (as it is

presently happening in Sweden) would read in that a serious plea, on the side of policy makers, towards a high level of employment and towards expansion.

(7) The extent of direct measures for special job creation programmes, and not only their evaluation criteria, should be agreed at the international level, since the fiscal adjustments, that such measures make necessary to adopt, could reverberate upon prices and, thus, upon relative competitiveness. Because of this, the best way, and the one to be pursued in the longer run, would be to finance such measures by an increase in indirect taxes (value added, or an additional tax on consumption goods), which would not be borne by exported commodities; however, this might be inconvenient in the shorter run, since it could contribute to develop a pressure on prices in the moment when expansive policies begin to take off, which would be undesirable.

(8) More in general the efforts towards expansion through macro-policies and towards additional employment programmes should be differentiated among countries. The rule for such a differentiation should be established in advance and made to apply quite automatically. Such a rule should be linked to some indicators of the trend of trade imbalances within the group of countries participating to the agreement, so that those which tend to have a surplus in their balance of trade with respect to the others should be those which are bound to practice more generously both expansive and job creation policies. This attitude could become contradictory in the longer run, since such policies positively contribute to growth, welfare and productivity. It will be odd, thus, to limit the benefits that the weakest among the partners could get. However, it is a sort of 'must' at the beginning, when the risks and the possible costs, in terms of inflation and above all in terms of international imbalances, are higher. Because of the same reason it would also be better that the extent of such policies be larger for those countries which have a higher trade surplus and a lower rate of inflation in absolute terms.

(9) A good way of weakening the effects of the contradictions described under (8) would be that of reconverting the use of European funds, in such a way as to make more resources flow towards the countries which have higher unemployment rates or infra-European trade deficits.

(10) A further important implication (the ninth one) is that the whole group of agreeing countries should aim at reflating the foreign demand for the goods produced within the area. This can be pursued by two coordinated sets of measures. On one side providing a system of guarantees and loans aimed at fostering the trade between the area and a relevant group of new developing countries. On the other side by promoting long term contracts between such countries and pools of firms belonging to different countries within the area.

(11) More in general, the whole of agreeing countries should promote a 'fair' degree of competitiveness with respect to the rest of the world, meaning by this the fact that the ability to compete should not be based, as it tends to be presently, on the erosion of labour standards and on the compression of wages, but rather on systemic efficiency, on the maximum exploitation of intelligence and culture, on well planned industrial coordination policies aiming at the valorization of the complementarities and synergies which appear to be potentially available within the European area.

(12) This requires to devote the maximum of efforts in favour of education and research, while deeply revising the presently prevailing tendencies favourable to low-profile training policies. Such policies, in fact, while possibly effective in the short run, not only reduce employment but contribute to make the system more rigid, since the tendencies towards continuous innovations tend to make any specific skill rapidly obsolete. Education, on the contrary, tends to make the labour force potentially more flexible and to mold the social environment in such a way as to become more creative and ready to accept innovations and their fruits. This does not imply skipping training activities, but rather avoiding to overstress their role and importance, shifting resources from training to general and higher education, making training vicarious to education.

(13) Many of the previous policy suggestions require a real leap in the quality of public action and, therefore, in intelligence and culture of public administration. Many of the suggestions imply also a widening of state intervention. Should the extension of the traditional sphere of state intervention and the quality of public administration remain as they presently are, the emergence of a negative attitude towards the proposed measures among ordinary people, mass media and politicians, would be likely to occur. This is why the whole of the proposed measures have not only to be accompanied by, but rely on, a profound revision of the philosophy of public action. The range of direct interventions should narrow, while that of regulation should widen; the state should directly do less things and become more capable to order to do things to third parties and to control that they properly and timely comply to such orders; in short, thus, less 'doing', and more 'regulating and controlling'.

In the first two sections of the chapter we have provided a synthetic and condensed exposition of the basic structural characteristics of our suggested guidelines. In the following ones we shall reconsider most of these suggestions in a more detailed way and in a more relaxed style. We hope that some inevitable repetitions be compensated by better understanding.

3. The basic rationale of the need for solidarity

Even if there is no moral solidarity between the nearly related races of Europe, there is an economic solidarity which we cannot disregard. Even now the world markets are one. (...) This is to put the issue on its lowest grounds. There are other arguments, which the most obtuse cannot ignore, against a policy of spreading and encouraging further the economic ruin of great countries. (J. M. Keynes, *The Economic Consequences of the Peace*, 1919)

In the previous chapters of the Report we have provided a description of the process which led to the present situation, that is essentially characterized by most Western countries playing a 'negative-sum game': gains in the short run are more than offset by losses in the longer run.

The present situation can also be depicted by saying that it is characterized by a very high degree of countries' selfishness. Each single country relies on the hope to achieve more positive results at the domestic level by shifting the burden of the present situation onto other countries: if the country is successful in achieving a higher productivity it becomes more competitive with respect to other countries, and enlarges its share of the world market; then it is able to rise its level of activity and, hence, its level of employment.

The difficulty lies in the fact that all countries are apparently following this same path and this puts the whole system into the 'negative-sum game': the increases in productivity achieved by every single country are not followed by a corresponding rising of its market share and, as a consequence, employment does not rise and unemployment tends to increase. The increases in productivity achieved by a single country can only produce positive effects in the short run, if the country is the first to experience such increases. At any rate, it is unlikely that temporary improvements in the country's market shares will imply a significant increase in the level of employment.

Thus, overcoming this situation seems to require, that all countries rely on solidarity, cooperation, and coordination much more than they are presently doing. In fact, the rationale which underlies our proposals is founded on emphasizing the social and economic relevance of solidarity, coordination, and cooperation at the domestic as well as the international level.

Our proposals aim to lead to positive-sum games, with countries/social groups earning in the medium/long run, although possibly paying some prices in the short run. Moreover, it is quite evident that the countries which should be bearing the heaviest burden in terms of losses in the short run are necessarily those that are better off in the current

situation. Thus, what we believe is required is a high degree of clairvoyance as opposite to shortsightedness. Only if countries prove to be able to go beyond the mere short period we can justifiably hope that the present critical situation will be overcome.

4. Towards coordination and homogeneity of policy: Some initial suggestions

The way toward a higher degree of coordination, co-operation, and homogeneity of policies among European countries can be made easier and more rapid if the Community itself gives rise to policies which go in that direction; in other words if it takes measures that can induce single countries to take the new approach to economic policies.

The Community could undertake a policy aiming to develop criteria for the evaluation of single countries' policies with respect to some pre-established and commonly agreed targets for all EEC countries (or groups of them). Here we shall simply outline some suggestions concerning job-creation policies. Our suggestions are articulated in a number of phases which may be distinct from the temporal point of view. There are four different steps: (i) acquisition of information; (ii) development of common objectives and targets; (iii) comparison between targets and actual performances; (iv) measures to be taken by the Community in response to countries' performances. Let us look at these aspects in a more detailed way.

(i) The acquisition of information. The Community could establish a sort of data-bank to collect data concerning job-creation in all country members. The information provided by countries should be about the outcomes of their policies in terms of new jobs created, in terms of expenditure, concerning the territory, sex and age of people involved. The outcomes are actual or expected according to whether a policy has been already implemented or has to be undertaken in the future.

(ii) Common targets. The available knowledge of employment and unemployment rates in all country members and the information on their past performances in terms of job-creation would be used to develop a common 'European' target concerning (a) the pursued decrease in the average European unemployment rate, and (b) the unemployment rates which each of the countries should seek to achieve in a certain span of time, consistent with (a). The availability of information is, of course, crucial. It is only thanks to detailed information that it is possible to fix 'realistic' targets, neither wildly ambitious nor excessively cautious. Furthermore, the common agreement on such targets would become a strong signal conveyed to firms, which should contribute on its own to create favourable expectations.

(iii) Comparisons. Once the employment-rate targets have been fixed, they become a standard to which the policies that each single country intends to undertake are contrasted. Thus, the policy options can be ranked according to their 'merits' in terms of job-creation.

(iv) Transfers, 'Rewards' and 'Penalties'. A further step - probably the most crucial one but that which presupposes already a good deal of solidarity - can be possibly taken: that of distributing European solidarity funds proportionally to the gap which exists between the actual unemployment rate of each country and the unemployment rate which is commonly stipulated for each country.

This system is such as to push each country, also those which are better off from the point of view of employment, to aim to further improvements in their employment situation; this would automatically imply, for the countries which are better off from the employment point of view, practicing more expansive policies, which is exactly what is correct to pursue. They can, however, choose not to do this, but then they will be implicitly obliged to transfer resources to the countries which are worse off from the point of view of employment. On the other hand, we have to recall that the targets - and, in particular, the envisaged decrease in the European average unemployment rate have to be commonly agreed. As a consequence of all these conditions, the danger of having inflationary pressures due to overambitious expansive targets is unlikely to emerge. This amounts to a system of transfers, but also to a system of implicit rewards and penalties. The effects of this kind of policy in terms of favouring a greater homogeneity among countries are quite evident.

5. The need for a new approach to macro-policies: To reduce the degree of uncertainty

For many reasons, most of which have been already considered, the traditional expansive policies do not seem to be able to give rise to those processes which should lead to higher levels of employment and income. What is required is policies based on a new and more advanced notion of what the public sector should do in a rapidly and deeply changing framework.

The traditional macro-policies which were followed in the late 1950's and 1960's, though successful in several respects, have never been completely Keynesian in their spirit. These policies, for a number of reasons, some of which have been recalled earlier, have successfully ensured an 'expansive framework' and a satisfactory enough control of business cycles by using fiscal and monetary tools but, in the all, state intervention has lacked one aspect which, in Keynes's spirit, should be regarded as essential and primary: the role that the state should play in market economies is to

contribute to lower the degree of uncertainty which inevitably characterizes them.

Uncertainty is an essential characteristic of market economies and it is the fundamental reason why the private sector is more likely to leave resources idle instead of using them to promote higher levels of production and employment. The level of income and, hence, of employment crucially depends on the volume of investment that is decided by the private sector (firms). Investment is a highly risky activity, it is made in view of profits and implies the transformation of liquid resources into fixed plants, machines, etc. whose perspective expected returns are uncertain. It is 'easier' not to invest and leave wealth and/or income in its liquid form (money and/or quasi-money). Investment, to a large extent, means to bet against the future. It is made in view of profits that depend on many variables which cannot be known and controlled in advance by any single firm or by a group of firms.

In this respect, the state has a very important role to play. Essentially it can create an overall climate (environment) in which private firms feel that to start new investment projects, to produce more, is less subject to the risk of being unsuccessful. The state can induce firms to form more 'optimistic' expectations and, then, to invest and expand their levels of activity. The state can determine the prerequisites for a future expansion of the productive capacity by the private sector.

Is the state playing this role in the current situation? Is it contributing, in other words, to reduce the 'structural uncertainty' which characterizes our economies? We must answer in the negative. It seems that most states are currently operating in the opposite way. Their actions and messages seem to be perversely intended to increase the overall level of uncertainty. Contradictory messages on the future budget policies, on fiscal and monetary policies, on sectorial policies and so on, coming from different representatives of the government or of the public sector cannot but produce higher uncertainty about what the state is actually going to do and about the context in which firms will be operating in the future. The recent developments at the international level provide further evidence to our arguments. The persisting state of uncertainty about what policies will be really adopted as to interest rates, rates of exchange, etc., magnifies the uncertainty in financial markets and, hence as an inevitable reflection, in 'real' markets.

In advocating a larger state intervention and the establishment of international institutions to promote a more ordered working of markets, Keynes had probably in mind a kind of national states and international bodies that probably is very far from those which actually exist. Keynes envisaged state apparatuses managed and controlled by committed professionals and politicians who give the highest priority to the general interest as opposed to self interest. In

reality, very different is the world: the conflicting interests of different national states, of different parties and social groups, of politicians, bureaucrats, lobbies, etc. all too easily lead to using the powerful national state apparatuses and the international institutions to serve special interests rather than the general interest both at the national and the international levels.

Perhaps, Keynes's vision of the state was much too simplistic, so that advocating an effective state intervention actually requires a much deeper and wider contextual analysis of how real state apparatuses work. However, we can draw a fundamental lesson from Keynes's works and concrete experiences. Twice in his life, Keynes faced very serious crises which involved the international system at large: the reconstruction after the two World Wars. In both cases he relentlessly worked to help develop policies to overcome those crises in such a way as to avoid the risk to have another one in a relatively short span of time. At the very basis of his indications there has always been the idea that solidarity was most required: to overcome the crisis no one (i.e. neither a single country nor a single social group) could possibly think of having the others to pay the whole cost and bear the whole burden of the crisis itself.

At least in the developed countries, the current situation, from whatever point of view, is not as dramatic as the one Keynes had to deal with. However, unemployment is a very serious disease which affects the social body in many ways, and the need for curing it is still great and pressing. Solidarity and more effective ways of state intervention are in order.

Solidarity, cooperation and coordination themselves are elements that strongly concur to the determination of a more stable environment, i.e. to reduce the degree of uncertainty. However, one should be very clear about the fact that these principles can be actually vehicles to get to a more stable and positive environment if they are freed, as much as possible, from ideology and lip service and become operative guidelines.

Historical experience has shown that many times, in spite of nominal commitment to solidarity, countries and social groups have acted in the opposite way, by trying to pursue their own special interests in the most ruthless way. If the need for solidarity, coordination and co-operation were to be interpreted in a merely ideological and abstract way, one could hardly expect any positive results stemming from them. Quite the opposite, mere lip service to these principles would engender more uncertainty in the form of mistrust and scepticism throughout the social and economic system. Thus, what is required is a genuine effort to follow the pattern of solidarity, co-operative and co-ordinate strategies, which imply taking concrete, rational and operative measures.

As a corollary to the foregoing, it is necessary to emphasize that the approach to new policies based on these principles must be characterized by moderation as well as by gradualness. Overambitious expansive policies (aiming to rapidly yield very high rates of growth) might easily produce perverse outcomes. On the one hand, too ambitious growth targets can ignite inflationary processes because they are likely to be inconsistent with the existing and available productive capacity in the short/medium run; on the other hand, especially in the present context, the more ambitious are the growth targets the more likely is that they are not trusted because they are regarded as unrealistic. In both cases, the result would be the ineffectiveness of the policy and its dismissal, with inevitable negative effects on the global expectations climate. Instead, cautious and gradual expansive measures would much more easily avoid the risk of failure, their moderation making them more credible and their gradualness allowing the system to adjust to the higher levels of aggregate demand.

6. Doing old things in a new fashion

As we have already pointed out, we need not only a policy which engenders expectations of a permanent expansive environment but also a policy which is able to efficiently ensure that the private sector responds to the stimuli in the 'right way', i.e. by enlarging capacity and employment.

In other words, the efforts directed to creating a permanent expansive framework do not seem to be a sufficient, though necessary, condition to induce firms to really take the path of growth. It is also necessary that the adopted expansive macro-policies are associated to measures at the micro-level which provide governments with the ability to check and influence firms' responses. Thus, 'old things' (expansive macro-policies) must be done in a new way. More precisely, traditional ways of stimulating private activity cannot be followed any longer and the new stimuli to aggregate growth must be associated to controls concerning their effects also at the micro-level.

Traditional 'Keynesian' macro-policies have been criticized for their lack of adequate and theoretically satisfactory consideration and analysis of the economy's micro-foundations. These criticisms, as well known, have led to new developments based on the so-called 'rational expectations'. Here, it is not possible to enter into a detailed survey and theoretical critique of this literature; but it is interesting and useful to concentrate on its policy implications, in order to contrast it with our viewpoint, which -though appreciative of the relevance of micro-aspects- arrives at substantially different conclusions with respect to policy.

'Rational expectations' approaches, with very few exceptions, arrive at the conclusion that public interventions

in the economy essentially represent disturbances which, as such, negatively affect otherwise rational (and satisfactory) market performances. It would thus be pointless - if not counterproductive - to try to alter the rate of unemployment that the market has established as 'natural' through macro-policies; in fact, their result will not be a lower unemployment rate but, for example, only a higher inflation rate. Keynesian macro-policies have not been successful because they have failed to correctly understand behaviours at the micro-level and, hence, how the private sector responds to the stimuli which come from the government.

Our stand is that traditional macro-policies have actually failed to cope with micro aspects in a satisfactory way but in a sense which is quite the opposite of the one just recalled above. The explanation of the failure of traditional macro-policies is not to be found in the fact that they represent disturbances of rational behaviours at the micro level. If they have failed it is because they have been unable to ensure that to the macro impulses engendered consistent and coherent behaviours at the micro level. In other words: there is no guarantee that private behaviours are rational, in the rather different sense that they are such as to always produce socially satisfactory outcomes; the public sector has tried to make up for this through its macro-policies but has not succeeded in making it sure that, at the same time, private behaviours were consistent and coherent with its objectives and goals.

What we have already said about the need to create expectations of a stable and permanent expansive framework is an example of what we mean. It is not sufficient to generate higher levels of aggregate demand to induce firms to behave in the 'right way', that is to say to expand their capacity and employment. However, to say that the overall degree of uncertainty has to be lowered to have firms to invest is not enough. It is necessary to find adequate ways to achieve these objectives and, most of all, the public sector must take measures that reduce the possibilities that the private sector (every component of it) responds in 'perverse' ways. In other words, what is required is measures and mechanisms which allow the public sector to control, monitor, and influence the private sector's behaviour, in order to 'force' it to follow the desired strategic paths. This can be achieved by adopting expansive macro-policies which are associated to micro-policies enabling the state to actually effect proper controls over the private behaviours, in order to have the private sector to respond to the macro expansive stimuli in a consistent way.

What does this mean in more practical terms? Here we do not pretend to provide full-fledged and well detailed policies, ready to be implemented by governments. But we can outline some examples of policies inspired to the need of creating a climate of stable expansive expectations and of having efficient and effective mechanisms to control market's responses.

The first example is given by new ways of rooting fiscal incentives. In what follows we develop two cases.

(i) Rewards to real output growth. Statisticians are familiar with the measurement of real output growth. Real output growth is measured through a ratio, the denominator of which is given by the value added in a given year, while the numerator is a more complex expression, that is the difference between the sales of the subsequent year deflated by an index of output price minus the money value of purchases of the same year, deflated by an index of inputs prices. Our suggestion is to estimate a similar magnitude at the level of firms, using this parameter as a basis for tax rebates. We are conscious of the difficulty of the task; however it can be performed exactly in the same way as estimating national output. It is difficult, but is usually done. The firms which are interested in getting fiscal benefits in this way, should declare the intention to do so, and collect, under the control of fiscal authorities and with the technical assistance of them, the necessary accounting information.

(ii) Rewards for the expansion of capacity. Although firms have their own notion of what constitutes capacity, this magnitude is difficult to be estimated by a third party. Therefore, one is obliged to use indirect evidence. One of them is given by the expansion of real output; however, in this case we are back to the scheme outlined under (i) above. Another way is to deduce this information by the actual increase in labour stock, under the assumption that an expansion of capacity is likely to require an increase in the labour stock. But this deduction is not necessarily true, since employment can be increased, also by maintaining the same level of productive capacity when the latter is, as it usually happens, underutilized. Furthermore, if there is an increasing capacity but this is associated to a process of substitution of machines for labour, the level of employment could remain steady or even diminish. Subsidizing an increasing employment, however, would not be a negative attitude in any case, given the high level of unemployment.

A third way is that of combining the evidence about an increase in employment with a rate of increase in the investment flows above certain target values (e.g. the average rate of growth of investment in the sector, a pre-determined arbitrary value, etc.). The increase in investment, however, should be measured in real terms; therefore, appropriate information about price indexes of capital inputs should be made available. Furthermore, a yearly rate of growth is not suitable for it could produce artificial delay of investments and a strategic concentration of them in a certain year, in order to have a rate of growth of investments larger than the established standard threshold. One way of coping with this difficulty would be to rely upon measures of average rates of growth in a period of several years, e.g. three years.

As to the way in which the state could positively affect private expectations, an example might be that governments make it known that it is their firm intention not to tolerate any longer levels of unemployment beyond a certain threshold, and that they will follow the required expansive policies to achieve such an objective. An illustration of a satisfactory policy of this kind may be the following. The government states in an unambiguous way that in the next, say, five years no rates of unemployment higher than, say, four per cent will be tolerated; (1) in order to achieve this objective, active expansive policies are undertaken. These policies, aim to expand aggregate demand and allow for 'rewards' (e.g. tax rebates, etc.) to the benefit of those firms which behave in the 'right way', i.e. they expand their capacity and labour demand in an efficient way.

As to the measures to expand demand, they have to be such that firms perceive that the increase in the demand for their outputs will be permanent and not erratic. To this purpose, the government could rely on a more extensive use of long-term contracts with firms -or, better, pools of firms- which supply goods and services to the public sector in connection with clearly stated long-term programmes. It is the long-term nature of the contracts and their connection to large long-term programmes which are most important, in that this strategy would more easily engender reasonably certain expectations for a relatively long span of time. The stipulation of a long run contract should in itself induce firms to widen their productive capacity; especially if the contract is defined in terms of things to be done rather than in terms of a given amount of money. However, there is the possibility that firms could play bets upon prices, contributing in such a way to the deflation of the scheduled expenditure.

The main problem is that long-term contracts usually provide clauses for the revision of prices. Such clauses can be utilized for betting upon prices and this should be avoided. The way out from this danger is given by the possibility of including in the contract clauses which reward, through appropriate fiscal rebates, behaviours which favour the increase in real output and productive capacity. The fulfillment of this target is possible, using the same mechanisms that have been described above with regard to possible fiscal automatic incentives to the expansion of real output. In this case, however, one could think also of the possibility to punish inflationary behaviours.

The firms, or the pools of firms, involved in contracts concerning long-run programmes, should accept a regime of special accounting, allowing for the informational control of the prices of outputs and inputs involved in the process of implementation of the contracts. The revision of prices

(1) This four per cent target could, for example, be established by referring to the 'European average employment-rate target' we envisaged above.

within the contracts instead of being based, as it is presently, on average price indexes, should be based on the specific prices involved and allowed only for the increases in prices of the specific goods and services which are bought by the firms or pool of firms in order to produce what is stipulated in the contract. At the same time, in order to encourage the contractor to make positive efforts to minimize increases in the prices of what is purchased, it should be stipulated in advance that in any case the compensation for inputs prices increases would not be immediate or complete. Obviously, this would reflect itself on the initial conditions of the contract, since the value of the contract will anticipate for this fact. This could apparently produce a higher expenditure but could also cause a larger saving in terms of the effects of price revisions. Therefore it is difficult to say whether the overall expenditure would be larger or smaller; however, the most important point is that, once the contract has been stipulated, the contractors will develop the maximum efforts to forestall the increase in the prices of their inputs. In other words, the state pays something more at the beginning, but from that moment onwards it can rely upon a diffused effort to keep prices as low as possible, and save money thanks to the smaller effects of indexation.

As we said, the contracts should aim at defining clearly the things to be done and the relative deadlines for their execution. This implies, on one side, that the projects have to be very well defined and allow for sharp controls of the qualitative and time features of the implementation process; on the other side firms could not speculate by attempting to exploit delays in execution to obtain price revisions. Apart from the effects in terms of stabilization of expectations, this will contribute also to increase the efficiency and effectiveness of public actions.

There are, however, other problems to be faced. First of all there exists the danger that the firms directly involved in the expansive process (the suppliers to the public sectors) are, to a large extent, firms which traditionally have relations with the public sector and are not necessarily the most efficient. These firms could have been selected because of strong pressures coming from interest groups, lobbies, clientele, etc. Secondly it could be argued that a significant flow of demand stemming from the public sector toward private firms negatively affects their efficiency and productivity. The existence of a reliable and stable demand might induce these firms to relax their efforts to improve productivity, whereas the competitive market environment would produce opposite, and positive, outcomes.

The government might deal with these difficulties -which are real- by selecting, for instance, only firms which, up to that moment, have been mainly operating in the private market and have demonstrated to be able to score satisfactory results

in terms of growth, efficiency, exports, etc. (2) The selection of firms according to this criterion would represent a guarantee that public contracts are not benefiting enterprises which, thanks to the protection of the public sector, are less dynamic and innovative.

As to the risk of engendering inefficiency in the firms which produce for the public sector, other mechanisms could be devised; for instance the government might draw contracts only with a single firm (or possibly with a consortium of firms) which, in turn, could partly contract out to others. In such a way there would be more guarantees that only efficient and competitive firms are involved in the process. In fact, it is in the interest of the firm which contracts out that the other firms are able to supply the demanded inputs or intermediate goods at the best available terms in the market.

In any case, of course, the government should carefully control the quality of the final product in order to avoid that the fulfillment of the contractual financial aspects is not achieved by lowering the qualitative standards of the goods and services supplied. If any firm proves unable - or unwilling - to conform to the established standards, the government should be empowered to break the contract, even though such a step should be taken only in extreme cases. Normally, the relationships between the public sector and the firms ought to be of such a kind that any deviation from the established terms of the contract and/or the agreement is rapidly corrected. This, of course, implies that controls, supervision, surveys, etc. do not take place only at the final stage of the process but regularly during the whole process, when it is easier, quicker, and less expensive to get 'things right' through adjustments.

(2) Of course, many different indicators could be chosen. For example the rate of growth of the value added, the number of new jobs created in the last year(s), and so on.

7. Some further remarks on the new public policies

So far we have concentrated on the relationship between the implementation of expansive macro-policies and the required mechanisms to ensure that they actually give rise to the desired results in terms of the growth of productive capacity and employment. This, as we have seen, implies new and different links between micro and macro measures, the introduction of more efficient forms of control and guarantee, etc. All this, though to a varying extent, represents a novelty in the traditional panorama of public policies. But a new and fresh attitude should be taken also toward a more general notion of state activities and expenditures. Such a new attitude too is related to the central importance of the links between micro and macro aspects and implications.

In economics we can identify three theoretical attitudes toward state activities and expenditures. They, though dissimilar from many points of view, share never the less a basic common inability to draw satisfactory distinctions between different sort of state activities and expenditures. On the one hand - especially among Keynesian economists - all kinds of state activity and expenditure are regarded as essentially similar: all of them, though possibly in differing degrees, have multiplicative effects on income; on the other hand - especially among economists more free-market oriented - all kinds of state activity and expenditure are regarded as essentially similar: all of them, though possibly in differing degrees, produce negative effects on the correct spontaneous functioning of the market. Therefore, the traditional Keynesian stand implies that state expenditure in general should be increased in order to promote the growth of income and employment, whereas the market oriented philosophy leads to the opposite conclusions. Finally, another viewpoint can be added to the two above mentioned, the radical/Marxist stand: state activities and expenditures are all 'unproductive' but at least some of them are socially necessary and therefore they must be expanded as much as possible to improve the conditions of those social groups and strata which are mostly damaged by the free functioning of the market.

In our opinion, all these three stands are unsatisfactory and theoretically flawed. Although we do not intend to dismiss the relevance either of the multiplier effects, or the distinction between productive and unproductive activities, or the social welfare implications of state activities, we believe that the three positions fail to perceive that public activities must also be differentiated according to their microeconomic implications.

The traditional Keynesian position appears to us too simplistic in its treatment of public expenditures as all essentially similar in that all produce multiplier effects. Even though it is true that, in the short period, whatever kind of expenditure determines similar multiplicative effects

on income, it is also true that different kinds of expenditure determine and produce very different impacts on the economic system, namely on the growth potentialities of the economy. Expenditures devoted to the development of scientific research, for example, produce longer-period effects which are very different from those produced by, say, transfer payments to households in order to maintain their income. Analogously, expenditures aiming to build new and more efficient infrastructures determine effects on the global productive capacity and productivity that are different from those created by expenditures devoted to final consumption.

The failure of the traditional Keynesian policies can be partly explained by their failure to correctly understand and evaluate the longer-period effects of public spending, with the result that the private sector responded to them in a 'perverse' way at the micro level. If we take also account of the unsatisfactory way in which expenditures were made (i.e. in a way which was not such as to create stable and permanent expansive expectations) our ability to provide a reliable explanation of the global failure of 'Keynesian' policies increases.

As to the market-oriented point of view, what is to be pointed out is that its advocates, in their drive to dismantle the existing state apparatuses, and to discard any form of intervention in the economic sphere -or, at least, to minimize its activities and influence- fail to perceive that some state activities and expenditures have indeed very powerful and positive effects on the private sector of the economy. Obvious examples can be made by referring to the effects of the presence of a large public sector on the functioning of financial markets: the very existence of public bodies contributes to reducing the degree of uncertainty in these markets. But many other examples can be made with respect to the 'real' sector.

Is it really possible to hold that the private sector of the economy would be better off if state intervention were indiscriminately reduced or abolished? Is it really possible to think that the private sector would be able to provide most of the infrastructures, utilities, public goods and services now supplied by public bodies and agencies more efficiently, or even with the same efficiency as the public sector? Not even Adam Smith, the most radical critic of the state's interfering in economic matters, was so certain of the possibility and convenience of leaving all the economic activities of the state to the private sector.

It is necessary to recognize that a wide range of state activities and expenditures, far from being merely 'unproductive' and fetters to the market economy, produce strong positive effects on the growth potentialities of the economy, just by affecting the micro framework within which private firms operate. Efficient and effective infrastructural policies, expenditures devoted to promote scientific and technological progress, etc. can significantly

lower costs of production in the private sector and favour its growth, efficiency and profitability.

It remains certainly true that other state activities and expenditures are 'unproductive', in that they may imply a subtraction of resources from agents which would use them to increase production, productivity, and efficiency. These 'unproductive' activities may be necessary and socially unavoidable but, never-the-less, they represent 'drawbacks' from the economic point of view. Thus, we arrive at considering the last stand, the radical vision according to which, in spite of their being unproductive, state activities and expenditures should be expanded as much as possible for social, political, and humanitarian reasons. If it is true that the principle of solidarity itself implies that the state has to perform functions of this nature, it is also true that the economic impact of the state cannot be forgotten or overlooked without producing significant negative effects on the growth potentialities of the economic system, which ultimately determine the size of the 'pie' to distribute in the most equitable possible way. Although the state cannot avoid to perform its 'social duties' and to carry out also unproductive activities, a correct and satisfactory balance between the two aspects of its intervention should be maintained.

It is from this point of view that we advocate new forms of state intervention. It is not as much a matter of finding out new areas or new activities as that of looking at already existing activities with a fresh attitude, by paying more attention to the issue of the relationship between micro and macro aspects and implications of the policies to be implemented. We believe that such an attitude would allow us to avoid the shortcomings of the positions recalled above. It is possible to escape either the temptation to carry out indiscriminate expansive policies merely based on unqualified increases of public spending, or to follow the ideological chimera of a pure market economy with destructive consequences at the economic and social levels, or to provide only assistance to the disadvantaged strata, which is an ultimately ineffective and self-defeating path to follow.

The need for taking this different attitude toward state intervention is made more urgent by the development of our societies. Not only is the current situation still characterized by excessively high unemployment rates which require effective and efficient policies to be undertaken, modern economic systems have also reached such a high degree of complexity and sophistication that more complex and sophisticated policies are in order. Let us consider, for example, the problem of environment and pollution. For a very long time, the progressive degradation of our natural environment has been regarded, more or less, as a sort of inevitable price we had to pay to economic growth and welfare: growth implies industries; industries 'naturally'

are polluting. Correspondingly, to intervene to prevent such a degradation, or simply to mitigate it, has been regarded as a sort of 'luxury' (i.e. an unproductive activity): to fight pollution might improve our living standards and, in some cases, is inevitable to limit the 'freedom' of polluting agents, but so doing we put obstacles to growth, employment, etc. In other words, a trade-off between growth and a pollution-free environment is assumed.

Is it correct to assume the existence of this trade-off? Is it really unquestionable that to fight natural degradation implies to fetter economic growth and welfare? There is much evidence to suggest that interventions to stop, mitigate, or eliminate the progressive destruction of our environment are not only necessary to defend human race from self-destruction but that they, in the medium/long run, can be also efficient and productive from a mere economic point of view. For example, to limit the degradation of sea coasts only apparently means to slacken the growth of the tourism industry. If the degradation of coasts is not stopped, eventually more and more spoiled coasts would not appeal any longer to holiday makers, and this obviously would imply very negative effects for the industries which rely on tourism, recreation, etc.

To fight pollution and natural degradation is not a 'luxury' which our societies cannot afford, especially in the present situation. It is just the other way around, and the state should intervene in this area much more heavily and extensively. In this way public activities would produce positive effects on the economy as a whole and, more specifically, would imply also higher levels of activity and employment in those productive private sectors which are paying growing attention to the environment (e.g. industries involved in recycling refuses, alternative technologies, etc.).

Another example of new possible approaches to the issue of state intervention and activities concerns the area of professional training. In this field, since a long time ago the need for some forms of public intervention has been recognized, so that our suggestions are mainly concerned with the need for new approaches to the issue rather than with the need for the intervention itself. Public intervention to provide professional training is regarded as 'productive' and efficient only if is distinct from education in general. Professional training to specific jobs is regarded as alternative to general education. But do modern societies, increasingly characterized by high flexibility and mobility in the economic sphere, actually require such a form of professional training? In a world in which workers are more and more required to adjust to new productions and technologies which keep on changing and developing at a very fast pace, the traditional professional training does not seem to represent any longer a positive or useful public contribution to the process of production and reproduction of the labour force. A kind of activity which might appear as

very much oriented to favour productivity and economic efficiency has become in reality obsolete and 'unproductive'. More general forms of education, more adequate to respond to the need of mobility and flexibility could prove far more 'productive'.

8. The need for a change in the philosophy of public action:
Less direct intervention and more regulation and control

In emphasizing the need for more effective expansive policies we are also advocating a more pervasive state intervention in the economic sphere. If, on the one hand, we share a critical attitude toward past policies and state actions, we, on the other hand, do not intend to translate this concern into an uncritical exaltation of the market and private behaviours. We believe that a correct balance between micro and macro-policies should be based on recognizing that macro-policies cannot be successful if they do not take proper account of individual responses. The latter, however, are not at all necessarily rational or socially acceptable, so that what is in order is, first of all, to endow the public sector in general with the adequate policies and tools to carry out an effective control of these responses.

We acknowledge, however, that our arguments might be objected by pointing out that there is no necessary reason to believe or to hold that the public sector behaves in a rational and socially acceptable fashion either. How can we be sure that public decisions and policies are actually more rational and satisfactory from the social point of view? Cannot these policies be crucially influenced and biased by particular vested interests (politicians', bureaucrats', clienteles' interests) as much as private decisions and actions are? There are no a priori guarantees that public behaviours are socially preferable to the private ones; a conception of the state which should predicate such an a priori superiority of the public sector would be either too naive or suspiciously partisan.

People are increasingly unsatisfied with public interventions. Dissatisfaction concerns both regulatory activity and the sphere of the direct production of public goods and services. As to the former aspect, people complain the excess of rules and their excessive formalism. They complain at the inability of public goods and services to effectively satisfy their needs, at the inefficiency and the wastage which characterize the process of production of public goods and services, at the unnecessary complexity of procedures to follow to have access to them, at the vexacious attitudes of the bureaucrats.

We think that the reaction against regulations is a very specific and limited case of hostility, basically inspired and 'inflated' by few powerful lobbies acting in a limited number of sectors, like telecommunication and transport. The 'deregulation campaign', led in the ordinary press by such

lobbies, found a wide sensitive audience only because people were fed up with the dissatisfaction they had concerning the sphere of public goods and services.

If we are right, as we think we are, we should devote a good deal of attention to the issue, since many of our proposals envisage a wider role for the state; thus, unless this is accompanied by a tangible contextual change in the ways in which the state behaves, not only with respect to the new tasks but also with respect to the traditional ones and its normal performance, an upsurge of negative political reactions is far from being unlikely. We devoted enough attention, in earlier chapters and Reports, to the main causes which generated a growing gap between what people would like the state to do, and what the state actually does. What we need now is to find the key for a more profound re-thinking of the basic philosophy of public actions.

The state, due to its sovereignty, has both the right to do things and to order that things be done. The tendency for the state has been, and still is, to choose mostly the first of the two alternatives. The simple reason was that it believed that it was easier to control what the state was directly doing, than to control 'orders to do' given to third parties. Historical experience has demonstrated that this belief was wrong. On one side the political process is not usually able to ascertain and identify the needs, their articulation and processes of changes, nor is it able to find the appropriate responses to them in a systematic and satisfactory way. Furthermore, also in the case of the state, there is a distinction between the subjects who give the orders (the government, the parliament, the ministries, etc.) and the agencies (organizations operated by civil servants) which have to implement the orders. Civil servants and the organizations themselves are endowed with their own specific cultural attitudes and interests and, therefore, the process of implementation of the juridical orders given to them might be, and usually is, variously distorted. The state, up to now, has not been able to learn to control itself.

Once this is fully realized, it is obvious that the choice between 'doing' and 'ordering to do' has to be made on other grounds, that is, on the basis of the better and less expensive fulfillment of the envisaged goals. The problem of controlling the fulfillment of the orders exist in both cases. It has to be faced as such with appropriate strategies, and must not be eluded, as it has fundamentally been until now. It is our opinion that in modern economic systems the need for a more pervasive and effective involvement of the public sector is not at all synonymous of its growth. The need for a more effective influence of the public sector over the private sector does not imply that the former should carry out more production directly. What is crucial is not the legal form of ownership (public *versus* private) but the ability and possibility to control and influence strategic areas, sectors, and activities within the system.

What we need to do, in other words, is to develop a new culture of control. Should this need be fully understood and accepted, and the culture of control developed, completely new possibilities would be opened to state action. The 'provision' of collective goods could be separated, whenever suitable and convenient, from its 'production'. The effectiveness of the process of satisfaction of needs would be guaranteed not by the fact that the state directly produces such goods and services, but by the fact that the state is (has become) able to control that the pursued objectives are met, independently of whether the state is directly performing the job or is delegating the concrete production process to third parties, in particular to firms.

In this new context, civil servants would increasingly become agents of direction and control. In other words, they would increasingly specialize in the intelligent tasks, delegating the purely executive and material tasks to others. Public organizations would become increasingly flexible and would increasingly perform mainly intelligent roles, in collaboration with third parties, which would, in any case, be subject to effective and penetrating controls. The state would increasingly become a 'buyer' of specialized goods and services, that would 'provide' to the collectivity through the budget, but avoiding or limiting direct 'production' activities.

The main tool to implement this change of philosophy is given by specialized contracts. The precise performance which is required by the state should be defined very carefully and specifically. And this should become the object of a contract proposed to external agents, put in competition each against the others. In the same way as the state is now accustomed to subcontract the building of a road or a bridge, it could subcontract many other activities, having defined qualitative standards and under the condition that it is able to control the correct execution of the contract.

This approach has also some relevant and more direct implications on job-creation policies. To the extent that the public sector becomes a 'buyer' of goods and services supplied by private firms, it will obviously become also less involved in the process of direct creation of jobs. But this is only a first aspect of the implications on job-creation. In fact, the public sector will continue to provide a more or less wide range of services directly, that is to say to use labour directly. This, however, in our opinion, should not imply to create permanent and, in many cases, very little flexible public jobs.

In the same way as the state buys goods from firms without establishing permanent relationships with them, it could choose to hire workers on a temporary basis in order to carry out specific projects with specific objectives (e.g. the provision of certain services, in a certain area, at a certain time). The public sector, should be careful to make it very clear that the jobs so created are indisputably

temporary and that in the future no measures will be possibly taken to change their nature. Furthermore, the state should use the above described 'technique' -based on contracts with third parties (firms, cooperatives, special independent agencies), the content of which is made by 'orders to do' things- in conjunction with with orders concerning 'how to do' things; the clauses on 'how to do' could indicate also how many unemployed, of what kind, for how long, and at what conditions, have to be hired in order to do the things that must be done, all these features having to be complied in order to fulfill the obligations of the contract. The gains in terms of more flexibility and mobility -both in the public sector as such and in the labour market in general- are evident while, at the same time, the impact on income, employment, living standards and social productivity are substantial. The jobs so created would have multiplicative effects in any case, and the services provided through them would contribute to increase living standards of the population and/or the productivity of the economic system.

What about the workers already employed by the public sector? It seems to us that a policy aiming at a substantial and rapid reduction of their number would be hardly practicable and socially unfair. The way to follow in this respect should be that of making serious efforts to improve the qualitative standards of public employees in order to make them able to better carry out the new tasks which the public sector is called to perform. For example, it is clear that to undertake tasks such as controlling, monitoring and surveying firms' behaviours and performances requires a number of skills and abilities which civil servants quite often do not possess. To play these roles requires familiarity with industrial and financial accounting, a wide knowledge of law, rules, etc., managerial initiative, and so on. A thorough and serious programme of restructuring and retraining public employees would significantly contribute to creating or improving these skills and abilities.

9. The need for cooperation and solidarity: The international level

In the previous sections, dealing with the expansive policies that we consider more suitable to the present situation in most European countries, we carried out our reasoning without paying much attention to the spatial framework in which these policies should be implemented. In fact, in many cases we have referred to single countries and national governments. This is hardly surprising: in the present situation most policies - regardless of their nature - are designed and implemented at a national level. In spite of quite a frequent acknowledgement of the need for a higher degree of international coordination, countries essentially continue to carry out their policies in isolation or, even worse, they are tempted by the 'chimera' of protectionism.

However, it should be clear that the kind of approach to expansive policies we have suggested necessarily presupposes a certain degree of international solidarity, cooperation and coordination, as we have pointed out since the beginning. In fact, it is quite evident that no single country can possibly hope to be really successful in the implementation of the policies above if there is not a reasonable degree of international cooperation. The adopted expansive policies create or worsen external as well as internal imbalances if a country is left alone to try to solve the problems of growth and unemployment. Moreover, the policies we suggest are not only expansive; most of them are also such as to yield positive and 'visible' effects only in the medium/long run, so that it would be even more difficult for a single country - namely for politicians - to bear the inevitable imbalances which, on the contrary, would manifest themselves rather quickly.

Thus, it is not reasonable to expect that any single country will be willing to take an expansive path if it does not expect that other countries will follow the same sort of strategies. On the other hand, even though - for any reason - a single country decided to take an expansive attitude and started these policies, it seems very likely that the arising of serious imbalances will lead, sooner or later, to their dismissal. This would imply all the negative consequences that we already considered; in particular, the tenability and credibility of future expansive policies would be seriously prejudiced.

What is needed, then, is some form of agreement among countries to give rise to a co-ordinate set of expansive policies along the lines depicted above. And coordination requires solidarity in that it means that some countries have to give up some of their privileges to help other weaker countries overcome their difficulties. Solidarity is a moral as well as an economic positive principle, so that countries should be able to perceive the future advantages of being less selfish today in exchange for future benefits.

However, at this stage, to rely only on the force of moral values does not seem enough. There is much evidence that countries are not currently behaving in a satisfactory way from this point of view. Thus, some forms of control and guarantee should be introduced: the countries which accept to implement expansive measures should also accept that some automatic forms of control are introduced in order to ensure the persistence and consistence of the strategy adopted.

A possible scenario might be the following. European countries agree on implementing simultaneous expansive policies. They are initially successful: income and employment rise, but in some countries the rise in income and employment is associated to increasing external imbalances (balance of payments deficits) to the benefit of some other countries within the group. The latter are exporting more and more towards the former. The way to cope with such a situation may

be to have the advantaged countries to reevaluate their currencies in order to reduce their surpluses so that the disadvantaged countries are favoured. In order to have the guarantee that this would happen, the group of countries might agree in advance that no country's external trade surplus with respect to other countries in the group can exceed a certain threshold. Should this happen the surplus country must automatically reevaluate its currency and/or take other measures which yield the same result of reducing its surplus. This, of course would be a short-term measure: if the external imbalances are of a structural nature, then other more radical measures should be taken.

The foregoing, of course, is only an example. It is also important to emphasize that the measures taken to control and regulate rates of exchange (within and among economic areas) should essentially have the nature of a deterrence. If countries involved know that their possible attempts to break the agreements (being too 'aggressive' and non co-operative toward the other partners) will be frustrated by automatic and inescapable offsetting measures, they will be less induced to be non co-operative. It is for this reason that automatic measures are important. Governments might select a number of parameters and establish that as soon as these parameters reach predetermined critical values offsetting measures will automatically taken.(3)

There is another important aspect that has to be taken into account. If countries tend to implement homogeneous policies and fix common targets and parameters (e.g. a certain rate of unemployment which cannot be exceeded), it is clear that the countries which begin with a worse initial situation would be put under stronger stress and pressure to perform in such a way to fulfill their commitments. Other countries' solidarity, in this case, would be crucial. It could take the form of creating a pool of funds devoted to help countries encountering significant difficulties; the pool should be fed by transfer payments coming from the countries that at any given time are better off.

However, in order to overcome this kind of difficulties it is not wise to rely only on mechanisms based on solidarity. It is also necessary to be realistic and be aware of the fact that the chances of success of the expansive policies grow if they are decided and implemented in a careful and gradual way, just in order to avoid that countries have to suffer unbearable pressures and stress caused by having initially fixed overambitious targets. Gradual policies may be less appealing in that they offer less impressive outcomes in the short run; but certainly they help avoid the risk of being grossly unsuccessful and, then, they promise more

(3) For instance, some of the parameters selected by EEC countries might be: imports and exports (among EEC countries and between EEC and other countries); employment and unemployment rates (disaggregated with respect to age groups, sex, etc.); average wage-rates, etc.

significant, stable, and permanent results in the longer run. Moreover, gradualness concurs to increase the credibility of policies just because it reduces the risk of their failure. In other words, gradualness itself is a way to engender stable and permanent expansive expectations.

10. The need for cooperation and solidarity: The national level

Solidarity, cooperation and coordination are very necessary at the international level, but the importance of these principles at the domestic level too cannot be underrated. If social and economic parties respond to expansive policies in a 'selfish' fashion, merely pursuing their interests, no many hopes of success are left. Firms' responses leading to inflation, inefficiency, etc. would be as socially negative as unions' responses leading to excessive wage increases, more rigidities in the labour market, etc. On the other hand, also politicians' and bureaucrats' selfish attitudes - aiming to exploit the new expansive framework to strengthen their power, clienteles, etc. - would be damaging and socially negative as well.

These observations always apply, and probably lack of solidarity, cooperation and coordination partly explains the failure of past traditional expansive policies in several Western countries. But the need to respect these principles is even greater for the sort of policies we advocate. These policies, as we argued, aim both to promote the growth of income, employment and social productivity and to improve the qualitative living standard of the labour force and the population in general. (4) The efficiency and effectiveness of these policies crucially depend on the existence of a proper balance between the two different sets of ends. Lack of solidarity and cooperation can easily lead to breaking such a balance when a group is able to bias the adopted policy to pursue its own interests. As a consequence of this, inevitable economic and/or social tensions would arise: policies excessively favouring private firms may easily cause unions' opposition and social disruption; policies excessively biased in favour of welfare may fail to engender the required expansion of private investment and employment. The conflicting interest groups should realize that the only possible way out to the current situation is through a 'social bargain' which necessarily implies to give up some privileges and advantages in the short run in view of overall gains in the longer run.

If there is no a priori reason to hold that one particular party acts in a more socially satisfactory way and that, quite on the contrary, all involved parties are led first of all by the thrust to pursue their particular interests, it is only through cooperation and coordination - which, in turn,

(4) Policies like those concerning the environment, health, and education are good examples.

necessarily require social and economic solidarity - that conflicting interests can come to forms of agreement/bargaining that ensure the fulfillment of the general interest to the largest possible extent. Through co-operation and coordination any form of control can avoid to become merely oppressive (and, hence, ultimately ineffective) and be rather the result of common acceptance of new 'rules of the game'. In such a way, the controls exerted by the public sector would not represent arbitrary measures against the private sector but they would be agreed devices aiming to ensure that all parties respect what all of them have recognized as the best behaviour in a given situation. Within this framework, also the public sector would be controlled: the process of agreement/bargaining would provide the private parties with significant powers of control.

We do not pretend that to follow the suggestions above and try to give rise to the radical changes that they seem to imply is an easy and smooth process. Quite on the contrary, we are well aware of the great difficulties which such an approach is bound to encounter. However, there are also reasons not to be excessively pessimistic. On the one hand, there is the wide and increasing dissatisfaction with the present situation, which can represent a very strong incentive to change and to intellectual and political creativity in order to find new solutions; on the other hand, though partially, there are experiences made by some countries (e.g. the Austrian experience) which show that a strategy based on coordination and cooperation is tenable. In any case, we would like to end the Report by pointing out that difficulties should not be a justification to inertia and intellectual laziness. On the contrary, they should spur to more efforts to overcome them.

APPENDIX

We have to demonstrate that, if we call $dv = v_2 - v_1$,
 $dv/v_1 > U/N_2$
if it has to be $Q_2 > Q_1$. In fact this implies
 $v_2 N_2 > v_1 N_1$
Since $v_2 = v_1 + dv$, and $N_1 = N_2 + U$, we will have
 $(v_1 + dv)/v_1 > (N_2 + U)/N_2$
 $v_1/v_1 + dv/v_1 > N_2/N_2 + U/N_2$
 $1 + dv/v_1 > 1 + U/N_2$
 $dv/v_1 > U/N_2$

PROGRAMME FOR RESEARCH AND ACTIONS ON THE DEVELOPMENT OF THE LABOUR MARKET

"SITUATION DES JEUNES FACE A L'EMPLOI A L'ISSUE DES MESURES
GOUVERNEMENTALES VISANT LES PLUS DE 18 ANS"

**TO OVERCOME YOUTH UNEMPLOYMENT:
YOUTH EMPLOYMENT POLICIES AND THEIR
EFFECTS IN THE CASE OF SWEDEN**

National Report
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**TO OVERCOME YOUTH UNEMPLOYMENT:
YOUTH EMPLOYMENT POLICIES AND THEIR EFFECTS
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1. Youth Employment in Sweden: a Success of Employment Policy?

As in most OECD-countries, youth unemployment rates in Sweden showed a steady increase during the 1970s and the early 1980s. Though more and more young people continued to secondary education, the unemployment rate for those aged 16-19 rose from 4.3 % in 1970 to 10.6 % in 1982. Although these figures were fairly low in comparison to some other EC-countries as the UK or Italy, the increase in youth unemployment caused a lively debate among Swedish politicians and the general public leading to a variety of measures to curb youth unemployment and to keep young people off the streets.

Contrary to the majority of EC-countries in which youth unemployment - despite the efforts of governments to reduce unemployment - is still on the rise, the measures taken by the Swedish government effectively lowered the unemployment rate for youth aged 16-19 to 4.1% in 1985. This figure is still about 50% higher than the unemployment rate of the total working population 16-74, but is very close to the youth unemployment level during the 1960s and early 1970s and might be considered as a "normal" level of frictional unemployment for the age group concerned.

What then is the secret behind this successful struggle against the rise of youth unemployment in Sweden? Are there possibilities to export the instruments of an active employment policy for youth to other countries?

In order to answer these questions we need to give a fairly detailed description of the development of Swedish macro-economic planning with special attention to the labour market policies carried out in Sweden. Furthermore, we must speak about the cultural and historical background against which the Swedish youth employment policy has to be analyzed. In this context, the structure of the educational system and the enrolment in secondary education is of special concern, as differences in the organization of vocational training (either as full-time programme in the school system or as dual responsibility of school authorities and employers) create differences in the interpretation of national statistics and the instruments available to influence youth participation on the labour market.

A summarized description of the range of policy measures carried out and the organizational framework for these measures will enable the reader to evaluate the results of the policy and to understand the reaction to the policies among youth, the actors on the labour market and the general public.

2. The Active Labour Market Policy and Economic Planning in Sweden

As pointed out by many researchers in the field (Wickman, 1980; Axelsson et al., 1983; Berglind & Rundblad, 1978) there is a tradition in Swedish macro-economic planning to see labour market policy as the core of the planning system. Meidner & Niklasson (1973) showed that a number of secondary goals were linked to employment policies, e.g. individual social welfare, reaching a balance between full employment, price stability, allocation of resources, balanced income distribution.

The dominant position of the labour market policy within the process of macro-economic planning in Sweden can be explained by the unique combination of academic reasoning represented by names like Wiksell, Lindahl, Olin in the Stockholm school of economics, open-minded politicians like Wigfors and Myrdal in the Social Democratic Party and the actual need to overcome the depression in the early 1930s. Combined with an early acceptance of Keynes' ideas of an active governmental policy to overcome unemployment and depression, the economic success achieved by state intervention during the 1930s and the centrally planned war-economy of the 1940s led to the establishment of a Central Labour Market Administration (AMS) in 1948. The increased importance of AMS as a tool to achieve the political goal of full employment is reflected in the increase of resources given to the Labour Market Administration which rose from 0.9% of the Swedish GNP in 1959 to 3% of the GNP in 1977. (Wickman 1980, 99)

Another factor in favour of long-term macro-economic planning in Sweden derives from the importance of the big corporate sector which, according to Wickman (1980) along with the growth of a large public sector, can explain the acceptance of concerted guidelines for economic development and state intervention in Sweden. As both, large private corporations and governmental administration share the need for stable conditions to secure investments in new production lines or in social reforms, sudden disturbances induced by developments outside the country have to be counteracted by planned structural change and adjustments inside the country. A gentlemen agreement concluded between the trade unions and the employers association in 1938 formalized this common interest in planned growth and constituted the ground for a widely accepted policy of long-term planning and restructurization of the Swedish labour market.

Named after the economic experts of the trade unions, Meidner and Rehn, a model of labour market policy was adopted from 1950s onwards, that not only accepted structural change in industry, but actively tried to move workers from enterprises with low efficiency to more productive areas of economy. Combined with a "solidarian wage-policy" implying higher annual

wages for low-income groups, this produced a very low wage-differentiation after a period of 20 years, with ratios of 1:3 in public administration and 1:5 in private enterprises. As Swedish employees are unionized to about 80% and the wage-agreements guaranteed the same income-level throughout the whole country, a continuous process of structural adjustment in the direction of the most profitable industries and a decline of branches with low performance as e.g. the textile industry was the result.

But the application of the Meidner-Rehn model also meant a strife for centralization and advantages for large corporations which could adjust their modes of production to the newest technology. In order to identify areas of economic growth, long-term planning surveys were conducted regularly from 1948 onwards, which coordinated the forecasts made by private and governmental research institutes. Though the results of the surveys only could be seen as information and recommendations by independent economists, their wide acceptance as a guideline for corporate investments and governmental intervention almost created an institutionalized link between the government and corporations in Sweden.

The common interest in planned development also paved the way for a general acceptance of an active labour market policy by the Swedish government. The government was given the final responsibility to guarantee a sufficient labour supply to the corporations in times of economic expansion and for full employment of the labour force in times of recession.

Thus, instruments for interventions on the labour market and in restructuring the qualification of the labour force were created during the 1950s and 1960s under the impact of economic expansion within the Labour Market Administration. A variety of interventions as vocational retraining, relief-work, sheltered work, wage-subsidies and financial aid for those moving to other areas of work were supposed to ease the adjustment of the individual to the needs of a restructured economy and were the prerequisite for the acceptance of these transformations by the trade unions.

Furthermore, there was a common understanding to give priority to measures securing employment (work-option) instead of only securing the income of a person (benefit-option). Gainful employment was seen as the prerequisite of full citizenship in Sweden. The right to employment has not only been a goal for the trade unions and the Social Democratic Party, but has been a dominating goal for all political forces in Sweden during the recent 30 years. This shared belief in the importance of full employment has resulted in the acceptance of a high inflation rate, repeated depreciation of the Swedish currency and tight legislation securing the rights of the employees on the labour market.

3. The Current Structure of the Swedish Labour Market

In accordance with the societal goal of secured employment for everybody, Sweden shows the highest global labour force participation rates. From a population of 8.3 million inhabitants, 4.4 millions were in the labour force in 1985 and of the age group 16-74 76.6 % of men and 68.1 % of women were part of the labour force (SCB 1985:2). But the increase of persons active on the labour market has not been followed by a simultaneous increase in working hours. On the contrary, Sweden shows a decline in yearly working hours by 6% between 1970 and 1980, while the number of employed people rose by 10% during the same period.

The reason for this development has to be seen in a variety of reforms introduced during the 1970s and the opening of the Swedish labour market for part-time employment. Since 1978 the minimum holiday period is 5 weeks, there is the right for paid parental leave of 1 year, paid leave in case of a sick child up to 60 days per child and year, a legal right to reduce the work of parents to 75% without remuneration, a legal right for unpaid leave in case of further education and various laws regulating the right of leave for political and union engagements. On the whole, the dominating concept of full-time employment - 40 hours a week during the year over the active life-span - has been eroded. Mainly women engage in part-time employment, on average 31.5 h/weekly in 1984, but even men show a decline in working-hours and shorter spans of participation during working-life.

Also changes in the economic structure, e.g. a greater variation in production techniques or the liberalization of shops' opening-hours during the 1970s created the ground for a growth of part-time employment. Unions often were reluctant to accept part-time during evenings and weekends, but especially young women with children and students found it attractive to take on these jobs which paid up to 100% more than normal employment. Thus, concentrated shift-work during the weekend may pay as much as 5 days normal work during the week.

Part-time work, reduced weekly working-hours, prolonged vacation periods and the right to paid and unpaid leave for various reasons coincide very well with the cultural habit of Swedes to maintain a strong link to the informal or private economy. Hunting, fishing, berry-picking and gardening considerably contribute to the Swedes' daily consumption and as it is a tradition to build cottages by oneself, a large part of the population spends its leisure-time in a very productive way. (Ingelstam, 1979)

While the opportunities of the already employed labour force to vary their work-load in accordance with other personal interests increased during the 1970s, the introduction of the Employment Security Act in 1974 weakened the opportunities of persons outside the labour force to be hired for a permanent job. (Vogel, 1983) The Act, which almost established tenure-like conditions for those already employed, created a division of the labour force in what in Sweden is called A-, B- and C-markets.

The A-labour market is reserved for the well-educated and trained work force who have been able to obtain permanent positions. They can be said to "own" their work-places as they enjoy all the legal rights linked to employment, may take leave for various reasons and are, to a high degree, secured against being fired. Even if they are given notice in case of lack of work, they are the first in the queue for new jobs.

The B-market is constituted by those well trained and able to perform according to the demands on the market, but who have failed to obtain a permanent position of their own. They are hired for short-time vacancies and move between various jobs and fields of work during a long period of their lives. Many women working part-time and young people with low working-life experience are to be found in this B-group.

The C-market consists of those who cannot perform in accordance with the demands of modern working-life and therefore cannot expect to be hired on the open labour market, but have to rely on sheltered work or relief schemes run by public agencies. In addition, early retirement-schemes remove persons who no longer can fulfill the labour market requirements from this market. According to several studies, the number of persons on this C-market has increased considerably and exceeds overt unemployment by 3 to 4 times. (Axelsson et al., 1983; Berglind and Rundblad, 1978)

4. Youth on the Swedish Labour Market

4.1. The rise of youth unemployment in Sweden

The responsibility of the state for full employment and for a smooth transformation in times of structural change in economy was generally accepted by all groups in society. Therefore, instruments for labour market interventions already existed when the economic crisis with increased unemployment, especially among the young generation, affected Sweden in the middle of 1970s.

For a period of more than 30 years, the Swedish labour market was characterized by a shortage of labour which had to be compensated by immigration. During the same period both, the unions and the employers agreed on a labour market policy which not only accepted closing down non-profitable industries, but also facilitated structural changes directed towards a higher national productivity and by that towards a higher standard of living for all Swedes. For young people, the only problem was to get a qualified training which enabled the individual to adapt to the on-going development in economy.

"School was supposed to give a good education to everybody. Anybody with good education was thought to get a well-paid job. By that schooling would contribute to solve unemployment, to raise material standards, and, as almost everybody would attend the same school, it would produce the anticipated material redistribution in society."

(Adler-Karlsson 1983, 47)

To fight youth unemployment, one only needed to expand the training system and to increase the quality of education and vocational training. Consequently, all Swedish youth have to attend a comprehensive compulsory school until the age of 16 and in addition, an integrated secondary school providing both, theoretical programmes and vocational training was introduced in 1971. In 1985, about 98% of all 16-year-olds in Sweden started secondary schooling, 37% in theoretical programmes 3 years or longer and 61% in vocational training and 2-year programmes. While the vocational training offered during secondary education expanded, most other forms of training as apprenticeships or company training programmes disappeared.

But despite a rise in the quantity and quality of youth education during the 1970s, which lowered the general participation rate of youth on the labour market, youth unemployment became higher and higher.

Graph 4.1 about here

4.2. The Causes of Youth Unemployment

In Sweden, as in most other countries, various causes of the growth of youth unemployment were discussed among politicians and the general public. High cost of youth labour, low level of vocational training, lack of work experience and a low individual motivation of young people to obtain jobs were mentioned as causes, along with the external influences of a decline in economic growth. For a detailed discussion of the economic theories and the diagnostic debate see Bruno and Lindner, 1987.

In general, the demand for labour or the existence of unemployment can be explained by applying two concepts:

- a) Factors influencing the supply of youth labour as e.g. cohort-size, structure of schooling, qualification levels among youth, legislation concerning youth employment;
- b) factors influencing the demand for youth labour as e.g. economic growth, technological change, wage-levels, competition with other employable groups as women or migrants.

In the case of Sweden, the first set of supply factors had some limited influence on the employment situation of young people during the last decade. While the increase of the number of youth aged 16-20 augmented the competition for attractive secondary education and available jobs, the rise of secondary education lowered youth labour force participation and the existing industrial safety regulations made it more difficult to employ persons below the age of 18.

However, all these factors can neither explain the rapid rise in youth unemployment in the late 1970s nor the establishment of a secluded, publicly administered youth labour market. It is the change in labour demand that predominantly has led to the change in the youth employment structure. The decline of economic growth as an effect of the oil-crisis, structural and technological rationalization in industry and cut-backs in public services brought recruitment of new personnel almost to a stand-still. In line

with the stipulations of the Swedish labour market regulations, employers were obliged to give priority to the continued employment of already hired staff. Seniority rules, the principle of 'last in - first out' and the so-called natural decline of staff by retirement placed the burden of unemployment on the shoulders of the young, not yet established on the labour market. In addition, a rise in beginners wage-levels made young people without working experience less attractive on a labour market with a surplus of experienced older workers. (SCB 1987:2, 33)

Higher demands regarding the vocational training and qualification of youth, often mentioned as a limiting factor (ERS, 1986), have only marginal influence on the employment of young people. Compared to the already employed labour force, most young people have a higher level of formal education and vocational training, but still cannot meet the qualification levels required by employers.

The Swedish system of separated vocational training in full-time courses might add to the development of different sets of expectations among youth and their teachers or supervisors in schools, and the representatives of industry and commerce. Especially in times of fast technological change, vocational training in schools cannot keep up with industrial development, especially with the use of new technologies, e.g. working with the most recent computer generation. Prolonged vocational training might, on the contrary, lead to further adjustment and adherence of young people to the demand of the educational setting and result in a growing distance to the reality of the open labour market. (Hartmann, 1985) Improved relations between employers and local vocational training courses and a greater engagement of companies in the specialized training of young people are seen as a solution to bridge the gap between skills taught in school courses and skills demanded by the employers. (Andersson & Hartmann, 1986)

4.3. Public Programmes to Fight Youth Unemployment in Sweden

The steep rise of youth unemployment in the middle of the 1970s was interpreted as a temporary decline in economic growth by most politicians. Therefore, it was assumed that unemployment could be overcome by introducing short-term training courses and relief-work for the age-groups 16-18 who were mainly affected by unemployment and did not voluntarily prolong their education.

The prolongation of schooling, based on the assumptions of the human capital theories developed during the 1960s, has absorbed a large percentage of young people and steadily decreased youth labour market participation

in Sweden. While further education in the beginning had only been seen as investment to promote the future collective and individual development in society, it was soon discovered that prolonged education also was an inexpensive way to keep young people off the labour market.

As early as 1977, the local school boards were given the responsibility for labour market introduction and a follow up of the living conditions for those aged 16 and 17, and in 1980 the Swedish legislation transferred the total responsibility for young people under 18 from the Labour Administration to local school boards. (SCB 1987:2) The transfer of young people into the sole responsibility of the school, though the formal school-leaving age remained at 16, discloses the official exclusion of those under 18 from the open labour market. (Magnusson, 1981)

This step meant also an end to an era in Swedish labour market policy. From the 1930s onwards, there had been the trust that the Labour Administration was able to cope more instantly and effectively with the problems on the labour market than any other institution in society. But the rising costs for youth relief work programmes and expensive work introduction schemes forced the government to look for other solutions. This became even more urgent as more and more young people had found out that it was quite profitable in financial terms to leave school at 16 and immediately receive a guaranteed income (in 1975 about SEK 2500/monthly) from a relief-programme whereas the study-grant for continued secondary education was SEK 250/weekly in the same year. (Hartmann, 1977)

Table 4.1 about here

Table 4.1 shows a great variety in the kind of intervention measures, but also in the levels of remuneration paid to the individual participating young person and to the organizations accepting young people. The differences in payments become understandable if one bears in mind that the majority of young people covered by the programmes are those unwilling to voluntarily continue secondary education.

Even though the Swedish government in its 1980 "Youth Bill" had envisaged a 100% participation of all 16-17 year-olds in regular secondary education, in 1984 about 9% of all youth under 18 participated in some kind of external youth follow-up programme, administered by municipal school-authorities. As many youngsters are reluctant to stay in any type of prolonged schooling, special youth centres are created, where vocational training assistants, welfare officers and psychologists develop individual

schemes to overcome their resistance for further training or to find a possibility for the young person to enter the labour market.

According to several studies, most of the young people involved in these schemes would prefer some type of in-house- training, an apprenticeship system combining work and continued vocational training, as this would satisfy both, the need for a regular income provided by one's own work and the need for more and closer contacts with the adult world. Such a solution for youth tired of schools is also favoured by most organizations on the labour market, but the total number is marginal compared to the other types of intervention described above. The relatively high wage-level (about SEK 5000/monthly in 1986), the regulation of the Employment Security Act to accept these apprentices as permanent staff in the company and the absence of a dual system of vocational training and work might be seen as obstacles for the introduction of apprenticeship in Sweden.

Instead, youth employment limited in time, with its lower remuneration in 1985 comprised about 7% of youth aged 16-17 and is welcomed by many employers who get a high subsidy if they employ youth temporarily instead of hiring permanent staff. (SCB 1987:2)

Table 4.2 about here

With the dramatic rise in youth unemployment for those aged 18 and 19 to more than 11% during 1983, it became obvious that the measures contained in the Youth Bill of 1980 could not successfully bridge an only temporary employment gap. They just postponed overt youth employment for two years. The political response was the introduction of a law, effective as of January 1984, which guarantees all young people aged 18 and 19 at least 4 hours daily employment at regular, union agreed wage-rates. Work in the "youth teams" is organized by each municipality and financed by a state-subsidy covering not only 100% of the wage costs, but also taking care of parts of the administrative over-head expenses incurred by the local authorities. The work of the youth teams should not compete with regular employment in public services and the young people participating have to leave the teams if they are offered regular employment or reach the age-ceiling of 20 years. (AMS-Information, 1985)

At the same time other measures, especially relief-work providing for full-time jobs with normal wages were discontinued and the young people aged 18 and 19 were first referred to the youth teams. Statistics show that the programme has effectively cut overt unemployment and offers at least

meaningful work and training to otherwise idle youth on a rather low level of income for the individual (about SEK 2500/monthly), but also at a reduced expenditure level for the Swedish government. Since 1984, even jobs in the private sector can be defined as youth team jobs, but the scheme remained predominantly linked to the public sector, where budgetary cuts prevented a permanent employment for young people.

To stimulate the creation of new jobs in the private sector by recruitment subsidies and 'insertion-jobs', new schemes were developed in 1984 and 1986, but faced a number of difficulties as unions protested against the competition with normal jobs and the wage-lowering effects of the youth schemes as experienced in Great Britain. (Coffield, 1986) The other provisions for this age-group are of less importance, but a subsidy paid to "new entrepreneurs" for starting their enterprises might be mentioned here.

Table 4.3. about here

In 1984, the unemployment rate of those aged 20-24 was more than 3 times higher than the rate for those 25-64, but from 20 years of age onwards, no special programmes are offered for young unemployed persons. Instead, the general instruments of the Labour Administration are applied. That means that relief-work or retraining measures are connected with a remuneration enabling the participants of that age group to live on an average Swedish income level (SEK 5000-8000/monthly). According to labour market statistics, about 2% of the age-group 20-24 were engaged in relief-work, about 2.5% in labour market training, whereas about 5% were overtly unemployed. (AMS statistics, 1985)

The general schemes described above are complemented by some other 15 measures designed to meet the needs of certain disadvantaged groups of young people as e.g. the handicapped, migrants or youth with deviant behaviour or drug problems. In addition, there are local job opportunity schemes and benefits to match the conditions of local or regional labour markets, often combined with the financial or personnel support of local governments or the cooperative movement (for details see Hartmann, 1985).

5. The Outcome of Youth Employment Measures

From a merely statistical point of view, the result of the Swedish measures to curb youth unemployment and to keep young people in an acceptable social environment has been very successful. According to OECD-reports Sweden, along with Norway and Switzerland, was one of the few OECD-countries (not considering Luxembourg and Island), where unemployment in general was below 2.5% and where youth accounted for only 8% of the unemployed, as compared with youth unemployment amounting to 69% of total unemployment in Belgium, 48% in France, 32% in the FRG and 41% in the UK. (DN 87-10-01)

Yet, official statistics can only give a distorted view of reality as methods of defining and counting unemployment differ between the countries and, even more aggravating for an interpretation, the societal background and basis of evaluation of certain statistical data are not available. Therefore, I will try to evaluate the outcome of the Swedish employment measures directed towards young people by reflecting the Swedish debate on the effects of youth policies.

5.1. Continued education: Warehouse or qualification for the future labour market?

The rise of enrolments in secondary education from 75% in 1975 to 97% in 1984 was predominantly motivated by the need of a more skilled labour force meeting the needs of the technological revolution in the future economy. But in reality, prolonged secondary training - especially in the shorter two-year programmes with vocational training - has become an alternative to overt unemployment. While it is impossible to quantify the size of "pull-effects" in detail, the attractiveness of secondary training becomes questionable when compared to "push-effects", i.e. the lack of acceptable alternatives. The statement of 44% of youth in secondary training that they would leave school immediately, if they could obtain gainful employment, is an indicator for the warehouse or parking-space effect of secondary training in Sweden.

According to Adler-Karlsson (1983) it is an irony that just in a situation where distinct job careers are difficult to find and the future of employment opportunities is difficult to forecast even for specialists, young people are predominantly forced into specialized training. Instead of using the time of prolonged schooling for developing personal skills and to prepare young people to find a personal coping strategy for the problems of change and insecurity in society, they are forced into a rigid training programme

often leading to dead-ends regarding the skills required in future working life. In times of rapidly changing production techniques in economy, the concept of secondary vocational training based on the vocational structures of the past has become obsolete. Instead of allegedly receiving the vocational skills for a life-time job during 2-3 years of training, young people should receive an education enabling them to accept continuous learning in the future and to adjust to a non-linear process of training, work, and leisure time in the future. (ERS, 1986; Hartmann, 1984)

Prolonged secondary schooling comprising all young people up to 18 implies also a tendency to adjust to the rules of the educational system, to peer-group relations and to the development of specialized youth cultures which might be opposed to the norms of working-life and therefore hinder a smooth transition from school to work.

Even if jobs are available, there is a tendency among young people in Sweden to reject jobs in industry as they do not correspond to their acquired attitudes and aspirations. In 1987, the Swedish industrial employers association was forced to start a campaign in order to convince youth to take on jobs in industry though there are still young unemployed. (DN 87 09 30)

One of the causes for this increased distance between the aspiration of youth and the reality of working-life is attributed to the Swedish system of full-time vocational training in schools. Increased study-visits and new forms of dual responsibility of schools and employers for the vocational training are under discussions, as industries which have kept up their own vocational training schools do not have any problems in recruiting youth.

5.2. Youth Employment Schemes: A Risk for a Special Career

The main goal of the multitude of governmental interventions on the youth labour market was to avoid overt unemployment with idleness and high risk of desocialization and stigmatization of the young people concerned. It was also in line with the goal of creating jobs instead of merely securing income. Evaluation studies undertaken by the National Board of Education show that of those born in 1967 and enrolled in the follow-up activities of local school boards, 43% were continuing education or vocational training, 2% were overtly unemployed, 9% were engaged in other activities, whereas 28% had been successful in obtaining gainful employment. (SCB 1987:2, 39)

However, the evaluation also shows that the percentage of young people who are able to move from youth team work to permanent employment is rather small and the measures are more efficient in motivating reluctant

youth to continue to other forms of education. The tendency to 'lock-up' young people in the public system of an artificially created youth labour market is very pronounced. In order to avoid overt unemployment and a long duration of relief-work, young people tend to shift between different types of programmes and shorter temporal jobs offered by the Labour Administration, without being able to obtain a permanent job on the open labour market. They are caught in what might be called the *unemployment career*.

Graph 5.1. about here

While the governmental system of differentiated programmes directed to certain age-groups leads to a steady increase in wages received for the participation in schemes, the young people, after 10 years in the system, might still be at the same point: unemployed. (SCB-välfärdsbulletin, 1985)

The creation of a marginalized youth group outside the ordinary work force, perhaps even stigmatized and excluded from employment on the open market because of their participation in the public schemes, has been a special feature in the discussion of the effects of youth teams. Contrary to the younger age groups, it cannot be claimed that these 18 and 19 year-olds lack vocational training, are not fulfilling the requirements of industrial safety regulations and therefore are disadvantaged in the competition for work. But their failure to obtain gainful employment after secondary education in the field of their trade and placement in a youth team in the public sector gives them even fewer chances in the job competition with those employed on the open labour market.

While the average unemployment rate among the 20-24 year olds was 6.4% in 1985, those who had left youth teams the year before experienced overt unemployment amounting to 12% and in addition another 8% were engaged in new types of schemes. Although overt unemployment of youth has to be regarded as the worse alternative, the lock-up effect of the schemes is the natural outcome of the comprehensive system. (Fath, 1985)

As stated in a report of the Statistical Bureau of Sweden the transition from education and vocational training to the ordinary labour market is delayed by:

- placement in a youth team as the first measure taken by employment services,
- predominant creation of youth teams in the public sector which, as a result of budgetary restrictions, cannot hire more young people even if there is a demand for work,
- active search for a job decreases during placement in youth teams,
- youth team work replaces jobs on the open market.

(SCB 1987:2, 43)

The replacement of relief-work schemes and other former measures for unemployed youth aged 18 and 19 by youth teams only securing half-time employment was heavily criticized by many young people, as their ability to make a living of their own on the pay from youth team work decreased considerably.

Interestingly enough, the income from jobs in fast-food services in the USA, a source of job-creation mentioned in most USA - Europe comparisons, has the same effects for the young people employed as the earnings from half-time youth team work in Sweden: youth cannot make an independent living on these earnings.

Compared with the average population, the income development in the age-group 16-19 was 35% lower in Sweden in the period 1980-1984. Young people increasingly depend on the support of parents and relatives and cannot afford to establish their own household as they used to do during the 1970s. In addition, the young people are well aware that a placement in a youth team job does not mean real employment. As negotiated with the labour unions, youth team jobs should not interfere with the normal labour market and the hiring of ordinary staff in public services or private industry. In reality, youth team work does replace jobs, but due to the limitations of budget there is no chance to hire more staff in most public services anyhow.

Psychologically, the awareness of the intermediate role of the youth team work becomes an obstacle, especially for young people who do their job well and are highly integrated in the informal relationship with the regular staff. Irrespective of their own performance and the reactions among their work-mates, they have to leave their positions when there is a vacancy somewhere else or if they reach the age-ceiling of 20. (Hofren et al., 1986)

Remaining in different employment schemes over longer periods also facilitates the creation of alternative life-styles among certain groups of young people. They have learned to combine the limited income from schemes with earnings on the black labour market or with the exchange of goods and services in the private economy, especially in remote areas of Sweden where hunting and fishing still play an important role for the life-styles of the male population. As a side effect, these areas show a high surplus of unmarried males whereas women from the same age-cohorts have moved to the cities with better employment chances in care and personal services.

The experience of survival on a relatively high level of welfare even without permanent employment within these groups and the freedom to plan their daily activities without the restrictions of an 8-hour working day may erode the protestant work ethics still dominating in the Swedish society and lead to a new mix of temporary work, engagement in voluntary organizations and in peer-relations, welfare benefits and leisure which, in the end, might result in difficulties to convince young people to work. Especially if the work is not in line with the social expectations and aspirations of young people, companies experience difficulties in hiring young people.

The provisions of a welfare society have opened an alternative for some, though only a small minority within the youth group, who might come to the conclusion expressed by one of the respondents in a local survey:

"I cannot afford to take on gainful employment. I will run my own life. Youth team wage plus some side-earnings give me more flexibility and income than a full-time job."

(Andersson & Hartmann, 1986)

In times of decreasing availability of paid labour, it would be wrong to stop these new, innovative forms of combining welfare provisions on a low economic level with work in the informal economy or the private exchange of services. The goal of full-time employment in the traditional sense of an 8-hour working-day during 46 weeks per year and for almost 50 years of one's life cannot be reached in a society where everybody is expected to participate in the work-force. Alternative styles of work-organization, new combinations of private and paid work, combined with engagement in voluntary associations can be facilitated by the provisions of governmental employment schemes. The outcome will not only be an improvement for the individual well-being, but also create a climate for innovation both, in economy and in public services. The experience of local employment initiatives and alternative work schemes in Sweden and in a number of European countries does not solve the immediate problem of mass youth unemployment. Nevertheless, it can be seen as the nucleus of future develop-

ments and areas for experimentation with new forms of entrepreneurial thinking. (Hartmann, 1985; ERS, 1986) On the other hand, the plethora of employment measures also gives rise to a huge bureaucratic apparatus of administration with its own set of rules and objectives which might be rather distant to both the aspiration of individuals and the needs of society.

In a local study it was noticed that different employment measures within a municipality had led to the growth of competing organizations looking for unemployed youth and placing them in various types of employment schemes. If the same number of young people had been employed as ordinary staff in preschools and other municipal services, the public would have saved about 10% of the costs due to the reduction of administrative personnel within the schemes. (Hagberg et al., 1986) However, a transfer of resources to local authorities would also mean a transfer of power and steering-ability from central government to a variety of local decision-makers who rather follow their local preferences than keep in line with the economic planning interest on the national level. Permanent public employment would also include a higher risk of overemphasizing the role of public services and of preventing the available work-force to change over to growing sectors in private economy.

In general, the policy measures to avoid youth unemployment in Sweden have led to very low overt youth unemployment, a rise in secondary education and vocational training in schools, a further decrease in youth participation on the open labour market and a shift of problems from the teenage-groups to the twens in the age-brackets 20-24.

6. General Implications of Swedish Youth Employment Policies

Looking at the outcome of Swedish macro-economic planning and the interventions of an active labour market policy which tries to avoid overt unemployment by the massive creation of public employment schemes and relief-work, one has to acknowledge that the result has not verified the prophecies of the critics.

While Sweden has avoided mass unemployment, especially among youth, and the creation of the "new poor" with the negative consequences of individual marginalization and social disturbance, economic growth has been well in line with other European countries. During 1982 - 1987, inflation has been cut by 50%, the balance of payments has improved from -5,8 billion SEK to +27,0 billion SEK, the budget deficit has been reduced by 70% and the stockmarket is flourishing with a value increase of 350%. (Dagens Industri 87-10-03) Thus, low unemployment does not automatically lead to high inflation, as stagflation might occur even in countries with rather high unemployment. Economic growth cannot only be achieved by rationalization at the expense of the work-force, but might be strongly influenced by the agreement of employers, unions and politicians on the steps needed to increase production. The transfer of people from industries of low economic performance to areas of economic growth is eased by the existence of public employment schemes and the active intervention of government in the creation of future employment opportunities.

Though Sweden has succeeded in avoiding the most negative effects for the individual in cases of structural changes in economy, the transfer of the work-force from traditional parts of economy, e.g. the manufacturing industry, to public services where there is a demand for labour, is hindered by the existing structures of unions and employers, taxation, the unemployment insurance system and regional imbalances. The acceptance to pay people who are not working unemployment benefits instead of using the potential work-capacity of the unemployed for the demands of labour can only be accomplished to a minor degree by the employment schemes.

The schemes rather allocate the work-force in line with administrative preferences within the Labour Market Administration than to allow public agencies to directly hire staff with the help of the financial means allocated by the Labour Market Administration. While the administrative system of the Labour Market Board facilitates the central steering and planning of the national economy, it, at the same time, favours a national perspective on the employment situation as reflected in nationwide statistics on employment.

National statistics on employment often disguise more than they disclose the actual employment situation of a country. Regional imbalances, with lack of labour in rural areas and a surplus in densely populated parts of Sweden and a high demand for youth in industry and private services in the big cities are immense problems at present.

Sweden, with its large area and small population is currently facing a drain of youth to the big city areas which boom in economic growth. Housing, not jobs, is problem number one for young people in Stockholm, while youth in the north of the country have no problems regarding their housing, but fail to get gainful employment.

Campaigns by industry to attract more young workers, the prognosed growth of the building industry and private services will worsen these regional imbalances. Only new types of macro-economic measures, steering resources to remote areas can prevent a population crisis in large parts of Sweden.

Regional imbalance is only one indicator which points at a future dualistic development in youth employment. A rise in the qualification requirements by employers, the tendency to overestimate technical skills in relation to humanistic knowledge, wage-differences between workers in public employment and in high-tech industry lead to dualism on the labour market. The use of micro-electronics and robots in manufacturing opens the way to a future where fewer and more specialized workers can produce more and more commodities.

While this, in the traditional sense, productive part of the economy will employ a minority of the work-force, the majority will find a job in services, generally regarded as unproductive, resource-consuming parts of economy. The highly trained and productive work-force might not accept to leave a large share of their surplus to a demanding majority of low-productive workers in services and will demand a larger share both, in economic and political influence. A new labour aristocracy might evolve. In order to avoid a divided labour market, or perhaps even a divided society, there has to be a structural change of the education and vocational training system which does not trap people in certain trades, but will allow for the application and acceptance of constant re-training during a person's whole life-span. Furthermore, we have to rethink the whole value-system and ideological basis of work in modern society. The question, which type of economic performance is productive and which is resource-consuming has to be reflected against the background of ecological requirements, basic human reproduction needs and long-term effects of production-modes on the social structure of society.

Thus, macro-economic planning cannot stop at the goal of full-employment, but has to ask about the societal need of the work demanded, the outcome of the production-process both, in physical and social terms, and the possibility of alternative ways of organizing the work-force of each society. The results of the Swedish macro-economic planning process show very clearly that the economic development is not the outcome of an 'invisible hand', but the result of a concerted effort of all groups in society to combine their skills and knowledge in order to avoid economic and social decline and to promote individual and social welfare.

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STATISTICAL ANNEX

SOURCE: SCB-Statistics of Sweden, Yearbooks 1984-87

Social Indicators concerning the age groups 16-19 and 20-24 in Sweden 1983

Activity rate (total working population as % of total population)

age:	16-19	46,4%
	20-24	82,4%

The unemployed as percentage of the total population

age:	16-19	4,9%
	20-24	5,6%

Unemployment rates (the unemployed as % of the working population)

age:	16-19	10,4%
	20-24	6,8%

Ratio between rates of specific age groups and total unemployment rates

age:	16-19	3,0
	20-24	1,9

Students as percentage of total population

age:	14-19	76,5%
	20-24	23,2%

Heads of household as percentage of total population:

age:	20-24	80,0%
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Selected indicators concerning population, activity rates and employment in Sweden

Specific age groups as % of total population - 1981

under 15 years	19,1%
15-24 years	13,8%

Activity rates (total working population as % of total pop.) - 1984

total	16-74 years	52,6%	thereof part-time:	3,6%
females	16-74 years	47,2%	thereof part-time:	45,4%

Proportion of sectors of economic activity in total employment

agriculture	5,1%
industry	29,8%
services	65,1%

Employers, self-employed and family workers (as % of total employment) - 1984

7,7%

Employment in community services (as % of total employment) - 1984

44,7%

Inhabitants/employed in community services - 1984

5,2

Teachers as % of employed in community services - 1983

9,0%

Pupils per teacher (comprehensive and secondary education) - 1983

9,1

PROGRAMME FOR RESEARCH AND ACTIONS ON THE DEVELOPMENT OF THE LABOUR MARKET

YOUTH UNEMPLOYMENT

The Case of Austria

Helga Fehr-Duda

Walter Reiter

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1. Austrian Economic Policy 1970 - 1985

During the recovery of the world economy in the seventies Austria enjoyed a favourable position. The average rate of economic growth of 5.9% in the years between 1970 and 1974 was 1.7 percentage points higher than the the average rate of the European OECD countries. The rate of inflation could be kept under the European average. The rates of unemployment during the sixties and the early seventies was the lowest of the postwar period.

The rapid economic growth in Austria was not, however, as in other countries, accompanied by a "growth-euphoria". The scepticism towards the idea that economic growth could be sustained indefinitely is explained by the strong historical consciousness of the social-democratic government. Therefore economic and employment policies reacted early when faced with the economic stagnation of 1974/75. This rather special approach may be called the "Austrian way".

Because of these arrangements, but also because of better objective starting points, the effects on the labour market were small, although the world stagnation in the mid-seventies did not pass Austria without leaving its marks.

At this time the service sector had unsatisfied employment capacities. Therefore most of the job losses in the other economic sectors could be compensated for. In the public sector, new jobs were created as well. The lowering of income taxes as well as the reduction of the workweek to 40 hours were also part of the improvement of the situation in the labour market (Novotny, p.39).

But the most important reason for Austria's successful economic performance was its expansive use of financial policy. Although it was already apparent that the growth forecasts for the mid-seventies were too high, the spending programs which had been planned on basis of these forecasts were fully carried out. The growing deficit was financed by foreign credits.

The direct employment effect resulting from the increase of deficit spending is estimated at 0.5% to 1.5% of the total number of employees (Butschek, p.32).

But because of the length and intensity of the worldwide economic crisis this employment-orientated financial policy could not be sustained much longer. The increasing indebtedness became a serious problem. Since 1983 the consolidation aspect has received priority so that the net deficit may be decreased.

Another feature of the "Austrian way" was the use of incomes policy in order to prevent large price increases. The financial authorities tried to stabilize prices by a strict linking of the shilling to the German mark. But the Austrian government also had to face the negative effects of the price stabilisation policy. The optimistic growth forecast had led to high wage increases by the middle of the seventies. Because of this and the higher rate of inflation compared to the Federal Republic of Germany, exports decreased and imports increased. The consequence was a rapid deterioration of the balance of trades. The deficit rose from 5.6 Mrd. Schilling in the year 1975 to 26 Mrd. Schilling in 1976 and 49 Mrd. Schilling in 1977 (Scharpf 1982, p.476).

Because of the hard currency position it was impossible to transfer the increased labour costs fully to prices. At this time it became apparent that this development had to be changed. A new course of action was adopted which relied on moderate wage increases and not on fiscal contraction.

While average wages increased between 4.5% and 8.5% per year in the first half of the seventies, the wage increases strongly fell off after 1976. Therefore the increase of the average labour costs in manufacturing (which amounted to 15% in 1975) just came to 0.5% in 1976, considerably below the rate of inflation. The development of wage movements had now become rather an inflation-dampening factor without raising unemployment.

2. The "Austrian Way": The System of Social Partnership

The fact that Austria, in comparison to most of the OECD countries, was able to absorb the economic shocks of the seventies relatively well has caused many observers to speak of an "Austrian way". The core of this "Austro-Keynesianism" is the Social Partnership's incomes policy. Although in most of the European industrial states considerable economic recessions occurred in the seventies, with mass unemployment, real-wage losses and budget cuts Austria seems to have been spared. The economic crisis led to massive political changes in the countries concerned. This phenomenon may be called the end of the social-democratic era. Here again Austria seems to be an exception: in 1979 the Social Democrats won the election.

Social Partnership means the cooperation of employer organisations, unions and the state. The efficacy of the Social Partnership is seen less in a direct influence on the wage and price formation as such but rather in the implicit imperative to negotiate over these matters.

The Social Partnership came into being when the Joint Commission for Wage and Price Questions was founded in 1957. Since then practically all decisions on economic and social policy are prepared in a large number of committees where the "Social Partners" are represented.

An important field of negotiations is the annual wage setting process: Increases of minimum wages are bargained over collectively by the unions and the business associations. These wage increases are essentially uniform since they are based on the average productivity growth of the economy and not on the growth rate of certain sectors or industries. Also, a common forecast of the expected inflation rate is taken into account in the negotiations (Wagner 1985, p.192).

This wage policy is designed to prevent mass consumption power from differing too much from GDP. A side effect of this policy is the stability of the personal income distribution of the employed. Business profits and the incomes of the self-employed vary greatly depending on the industry concerned, because firms with productivity data below average are forced to achieve an increase in productivity growth.

In periods of economic prosperity, mostly the trade unions have gained from the system of Social Partnership. Certain variables which are normally determined by market forces here depend on a bargaining process which means a redistribution of power. Even strategic decisions which are elsewhere the sole right of capital owners have to be co-determined by workers in Austria. Therefore the initiative to keep the system of Social Partnership alive has mostly come from the unions (Marin, p.45).

Since the beginning of the eighties, which are characterized by stagnation and growing unemployment rates, the system of Social Partnership has been challenged (Gerlich/Grande/ Müller). One reason for this development is the crisis of the nationalized industries. These firms are highly concentrated either in sectors struck by the economic recession or in politically controversial sectors such as electricity, chemicals, and housing construction. Recently a large number of workers has had to be dismissed from the nationalized firms, which has led to a deterioration of the public sector's image.

The Role of the Government

In this system of Social Partnership, the government has a compensatory function: As long as the bargaining partners are prepared ex ante to conduct both wage and employment level negotiations with the intention of maintaining full employment, the state is prepared ex post to make up the costs for any imbalance in these levels.

This willingness to compensate, which is seen as a sort of "immanence" by business and the unions, is intended to promote business confidence.

Specific compensatory measures include the awarding of public contracts, subsidies of investment credits and direct support of jobs.

3. The Austrian Labour Market Agency

Labour market policy in Austria is determined strictly on a federal level and is pursued directly by an administrative authority, the Labour Market Agency (Arbeitsmarktverwaltung), under the supervision of the Ministry of Social Affairs. The Labour Market Agency has three levels of organisation: the Ministry, a regional employment office in each of the federal states, and the local employment offices. The ministry is responsible for the formulation and planning of labour market policy which is then carried out by the provincial and local

offices.

The offices of the Labour Market Agency are assisted by specific advisory bodies to ensure that the offices' activities reflect the interests of the Social Partnership. This informal consensual orientation has strongly influenced all of Austrian postwar labour market policies, such that, on an international comparison, there has been relatively little state regulation of the labour market. The decision-makers work the agreement that compromise on one level saves intervention on another.

The Council for Labour Market Policy

The Council of Labour Market Policy is the Ministry of Social Affairs' advisory committee within the Social Partnership. This council thus includes six members from each of the employer organisations (Chamber of Commerce, Association of Industrialists, Chamber of Agriculture) and employee organisations (Chamber of Labour, Trade Unions, Chamber of Agricultural Labour). It further consists of one representative each of the Chancellery, the Ministries of Finance, Commerce, Agriculture and Forestry, Construction and Technology, Internal Affairs, Education and Art, and Transportation and of representatives from the fields of economic and social sciences. This constellation is expected to represent the interests of the economy as a whole, which the state's labour market policy is equally required to support.

The council is chaired by the Minister for Social Affairs, a quorum is constituted whenever more than half of the members are present, and the resolutions are passed by simple majority. Although these resolutions are merely recommendations and thus not legally binding, Ministers have until now always taken their decisions in accordance with the resolutions. Analogous to this council, the other two levels of organisation of the labour market agency also have their advisory committees which decide in regional and local questions. The prime function of these committees is to gather information and to encourage contact and cooperation between businesses, employee representatives and local interest groups within each region.

There are several points which make the framework of the Labour Market Agency quite different from that of other countries. Especially the method of raising financial resources for active labour market policy should be mentioned. Virtually all of its means are drawn from the Unemployment Insurance Fund, which is financed through a percentage charge on wages and salaries. This levy, borne by employers and employees at equal shares, is fixed by the Minister of Social Affairs. In doing so, he cannot, however, exercise unrestricted discretion. He has to set the charge such that the estimates for incomes balance those for expenditures of the Unemployment Insurance Fund. The persistent slack of the economy since 1979 forced the Minister of Social Affairs to raise the charge from 2 per cent (1980) to 4 per cent (1983). However, most of this increase had to be spent on unemployment benefits rather than on active labour market policy (Pichelmann/Wagner 1984, p.215).

To realize its intentions the Labour Market Agency runs programmes which can be divided into four main types: training, employment creation (wage subsidies als well as low interest credit facilities), apprenticeship and youth training programs, and assistance to the handicapped.

The most centralized type is employment creation. In this area, it is the Minister and his special advisory board who direct the allocation of funds. The frequency and intensity of the use of labour market policy instruments vary according to the political situation. Policy measures can be amended and brought up to date when they are no longer appropriate to the problems at hand.

On the basis of such amendments, the Labour Market Agency then tries to plan the optimal use of instruments by integrating long- and short-term elements in its programme.

Each year a new list of policy measures is worked out to take into account both current problems and the implementation of long-term goals. The programme is examined and endorsed by the Advisory Council.

These policy measure programmes are viewed as declarations of intent and provide an orientation for the allocation of budget funds for individual instruments of labour market policy. For the authorities subordinate to the Labour Market Agency, they serve as an interpretation of current problem-saving strategies.

In the course of economic slowdown after 1975, more and more priority was given to the creation of employment opportunities, and the corresponding policy measure programmes were increasingly concerned with the problem groups of the labour market. Thus the Labour Market Support Law (Arbeitsmarktförderungsgesetz) passed in 1969 was amended eleven times by 1985 to provide for the creation of employment and the expansion of training opportunities. The ninth amendment of the Labour Market Support Law also provides for "self-help" facilities by which, for example, a bankrupt company is permitted to continue its operations under the management of its own employees, who would otherwise be faced with unemployment.

Further important impulses resulted from the OECD programme initiated by France in which job creation on a local level was implemented as a new area of labour market policy.

4. Social Partners and Experimental Programmes

The orientation of Austria's labour market policy toward consensus among the social partners creates a difficult environment for innovative and experimental approaches. The positions of the business associations are marked by considerable reservations.

Social-political motivation for employment creation measures is generally rejected, for the business associations feel that only profit-oriented businesses, rather than public services, can generate the investment required to create secure and productive jobs. Apart from the view that too much in public funds is contributed to state-owned companies and public services at the expense of the private sector, it is also postulated that an expanding non-profit sector is incompatible with a market economy, and that the Minister of Social Affairs pursues not only a pro-employment policy but also an anti-market policy. It is further felt that the support of "self-help" facilities has created a broad ideological field for testing the viability of anti-market economy models on the expense of society as a whole.

The position of the unions toward unconventional employment programmes is also rather reserved. They point out the danger of self-exploitation (for example, in the form of unpaid overtime) which is often accepted by employee-managed companies during an expansion phase in order to maintain their own jobs and to be able to compete with privately capitalised companies.

Employee representatives fear that a disregard for the collective bargaining agreements could develop into an instrument for weakening the labour regulations in the private sector, and they see the current debate over "self-help" facilities, in which conservative voices are clearly heard, as a confirmation of their fears.

However, the labour market policy function of "self-help" and the maintenance of jobs that would otherwise be lost prevent these reservations from developing into outright rejection. Unconventional employment programmes have already met with considerable success in specific problem areas of labour market policy and their relevance for the youth labour market is also implied in the statement that youth unemployment is caused by management's reluctance to hire young people. As this attitude on the part of management is not expected to change, a shift in the existing concentration of job creation programmes from the private sector towards experimental projects would also be in the interests of the unions.

5. Youth Unemployment

The youth unemployment rate was nearly equal to the rate of total unemployment until 1981 when the employment situation worsened rapidly. Since 1981 young people have been subject to above-average unemployment. While the unemployment rate of the whole economy was 3.7% in 1982, the rate of youth unemployment climbed up 4.1% and by 1983 was already up to 5.7%. (Biff1, p.10)

The proportion of the unemployed below age 25 in the stock of the unemployment register increased from 24.3% in 1980 to 28.8% in 1982, despite the fact that youth unemployment was not as explosive in Austria as in the other Western industrial economies.

A good indicator for the risk of losing a job is the ratio of the number of people becoming unemployed to the total number of employed and unemployed in a year. The figures indicate that young workers run an overproportional risk. It is interesting to note that it is especially the people between 20 and 24 years old for whom the probability of losing their job is highest. Since 1983 the 15- to 19-years-old people have also belonged to the high-risk group (see table 1).

Table 1
Ratio of the number of people becoming unemployed
to the total number of employed and unemployed in a year

	1980	1981	1982	1983	1984	1985
all people	9 %	11 %	14 %	15 %	15 %	15 %
15 to 19 years old	8 %	7 %	13 %	17 %	19 %	21 %
20 to 24 years old	12 %	15 %	20 %	22 %	22 %	23 %

Young people are also in Austria more subject to the reduction of employees in the whole economy because, in a recession, entrepreneurs try to reduce the labour force to the so-called "core" of the personnel.

The function of the "border staff" is in practice that of a potential for adjustments to changes in demand. Young people, especially those who are less qualified, often belong to that group because they are not yet integrated into the operational chains of mobility and promotion. The growing number of young people afflicted by unemployment and the declining chances to get a job again confirm the hypothesis that staff reduction always affects those people most who have worked in a firm for a relatively short time: Whoever comes last has to go first. (Pichelmann/Wagner 1984b, p.200).

The longer the crisis of the labour market lasts, the more the core of the personnel is also affected by staff reduction.

Enterprises change the labour force if they find more qualified persons on the labour market. "For Austria this process can be recognized by the fact that a growing number of the labour force from the middle of the wage and salary pyramid is affected by unemployment." (Pichelmann/Wagner, 1984b, p.195f.)

Nevertheless young people are more affected by a restrictive personnel policy on the part of employers. Operational training costs may be reduced as a result of raising the hiring standards. Corresponding training will not be offered on the job; rather it will be demanded that the employees bring along with them the necessary qualifications and job experience. These higher criteria and the required work experience are the barriers which handicap the entree into professional life.

The number of apprenticeships diminished in the years 1980 until 1983 from 197,000 to 175,000. The proportion of apprenticeships to the job market as a whole those sank from 7.1% to 6.6%.

Especially the situation for girls on the apprenticeship market has rapidly become worse. Besides that it may be assumed that many young people who are in search of jobs are not quoted in the statistics. As they have no claims to unemployment insurance payments there is no incentive to register as searching for a job. Estimates for 1981 (Butschek 1982) resulted in more than 7000 young people aged between 15 and 19 years out of work without being registered as unemployed by the labour exchanges.

6. Measures against Youth Unemployment

All subsidy measures for procuring jobs for young people aim at securing them long-term unemployment.

The Austrian labour market policy mainly consists of three kinds of intermediary subsidization in the field of private enterprise. In any case the amount of the subsidy must not exceed a maximum of seventy percent of wage costs.

Within the "company hiring subsidization plan" the potential employer receives subsidies of the wage costs. This aims at encouraging employers to create additional jobs for young people or to hire young people for jobs becoming vacant even if they are less qualified than other workers.

These hiring subsidies are very often connected with training support. If a company is prepared to instruct unqualified youth it may obtain a refund during the training from the Labour Market Administration.

These subsidies may apply to the initial acquisition of qualifications if the young person has no professional training as well as to youth with professional training but no experience. As a rule the hiring company is granted a training subsidy after presenting a corresponding training schedule which shows the reason for the measures, the necessary time, the contents of the programme and the expenditures.

In both cases a regular employment contract for the subsidized person is required. This is not the case for subsidies of the practical job training programme. In this case, though the subsidized person enjoys the full programme of social insurance, the employer does not provide an employment contract. Rather youth are offered the opportunity to participate in practical on-the-job training precisely because of the lack of a direct opportunity of procuring employment. Moreover they are offered an individual subsidy to cover their living expenses. The company does not incur any expenses during this time. If it later takes on the subsidized person with a regular employment contract, it enjoys the advantage of not needing the initial training period for a new employee.

This kind of measure is mainly intended for youth with completed professional training. Even if they do not always result in an employment contract, they provide an extension of training through practical knowledge and by that improve the future prospects of employment.

These measures for procuring employment belong to the traditional tools of active labour market policy. Moreover the Labour Market Administration tries to achieve a problem-oriented focus of the measures by special programmes. The largest of these special programmes is shown as follows.

7. Special Programme "Aktion 8000"

From 1981 to 1983 a development began to be recognized which was defined as "segmentation of unemployment": opportunities of unemployed to reenter employment have been increasingly unequally distributed.

For certain groups of persons it takes longer and longer until they find new jobs. Youth with no professional experience have been harder and harder to find jobs for.

The Labour Market Administration was therefore forced to develop employment programmes for both of these problem groups of the labour market. Thus, at the end of 1983, the "Action Programme to Create Additional Employment Opportunities for Youth and Long-Time-Unemployed", better known as "Aktion 8000", was launched. Since the beginning of 1985, due to difficulties of execution, only jobs with public and non-profit institutions may be subsidized.

The "Aktion 8000" is an employment programme which is exclusively concerned with the non-profit sector. Subsidies within the "Aktion 8000" are granted for the employment of

• youth (until the age of 25) which have been registered as unemployed for at least three months or are able to prove that they have been unemployed for at least three months;

- unemployed over the age of 25 with a minimum registration time of six months (long-term unemployed).

Youth may therefore also be subsidized if they are not registered at the Labour Office. With respect to the jobs offered and employment contracts certain conditions have to be fulfilled. Subsidies will only be granted if the participating employer takes all social welfare standards into account. This is supposed to prevent an implementation of precarious, i.e. legally not defined employment contracts with public funds.

In detail these regulations contain the following conditions:

- an employment contract lasting at least one year has to be concluded with the subsidized employee. As a rule, within this time period eight months will be subsidized, the remaining third has to be financed by the participating employer;
- The wage is supposed to correspond with the locally common level and must not be lower than the wage agreed upon in the Collective Bargaining Agreement;
- Within four months before the engagement and during it, it is not allowed to dismiss employees in the working field of the subsidized person without the agreement of the Labour Office concerned.

Project oriented measures:

The Labour Market Administration differentiates between individual jobs and project jobs. An individual job is given if the subsidized worker is integrated into an existing team and the field of activity of the participating employer essentially remains the same.

Thus it is also possible to establish more individual jobs at the same employer. It becomes more complicated with regard to project jobs. Translated into the language of the Labour Market Administration, the word "project" in connection with the "Aktion 8000" is only used if it will be founded in order to execute the subsidy programme. This means that project jobs are limited in respect of the volume of activity, the level of qualification needed and the time estimated. The jobs created for the project are therefore defined as project jobs. Public as well as non profit institutions may participate.

To ease the choice of the participants for the Labour Office the ministerial programme planning has given various suggestions for appropriate organisation forms. Specially qualified employers for the execution of project jobs with subsidies of the "Aktion 8000" are officially: communities, associate communities, forest authorities, local environment lobbies, citizens committees, women's centers, youth centers, religious institutions, social welfare centers, and so on.

Job projects which are created by these employers to execute the programme "Aktion 8000" are required to fulfill certain social-political criteria. Mainly within project oriented measures, the "Aktion 8000" aims at a combination of social and employment criteria. Project jobs are supposed to be created mainly in socially, ecologically and culturally critical sectors. Therefore the following fields of activities are said to be especially worthy of being subsidized: environmental protection, social services, municipal renovation, village improvement, culture and art.

Conditions of Subsidies

Also within project-oriented measures the subsidy is connected to the person. The conditions already mentioned apply as well. They have been extended to include three additional conditions:

- a direct project substitution within the fields of activities has to be impossible;
- by analogy with subsidized individual jobs the subsidized projects have to be additional ones, i.e. not to be realized without subsidy.
- the participation of other public or private authorities is required. This third condition may be dropped in the case of important projects.

8. Evaluation of the Programme "Aktion 8000"

Within an international perspective, the programme "Aktion 8000" can hardly claim to be "experimental" in itself. Similar schemes have been introduced in many European countries for some time. Nevertheless, from the point of view of the Austrian labour market administration, the "Aktion 8000" entails the necessity to adjust in an innovative fashion, for several features of this new programme do not go well with established procedures of active labour market measures. Two aspects stand out: First, the jobs are created in the non-profit sector; secondly, the jobs are of a transitional nature (they might be shed the moment financial support runs out).

Drawing on his experience, a seasoned administrator within the Austrian labour market agency would argue that the "non-profit" and "non-permanent" character of the jobs financed through the "Aktion 8000" puts the success of the programme at high risk: First, the programme has to be implemented on a local level, which causes frictions within the federal agency traditionally run in a highly centralized way. Given this tension between the organizational routine and the specific implementation prerequisites of the programme, the "Aktion 8000" will never really get off the ground, either because take up will be very low or because the central bureaucratic machine will grind to a halt if forced to deal with great local variations of programme administration.

Secondly, the non-profit organizations will behave in a counterproductive way; either they will carry out work traditionally done by a regular employed person through an "Aktion 8000" job, thus undercutting union rates; or they will give only menial work to those employed through the "Aktion 8000" (for the whole set-up is considered as merely transitional) thus depressing rather than enhancing the general capacity for work of the young and long term unemployed.

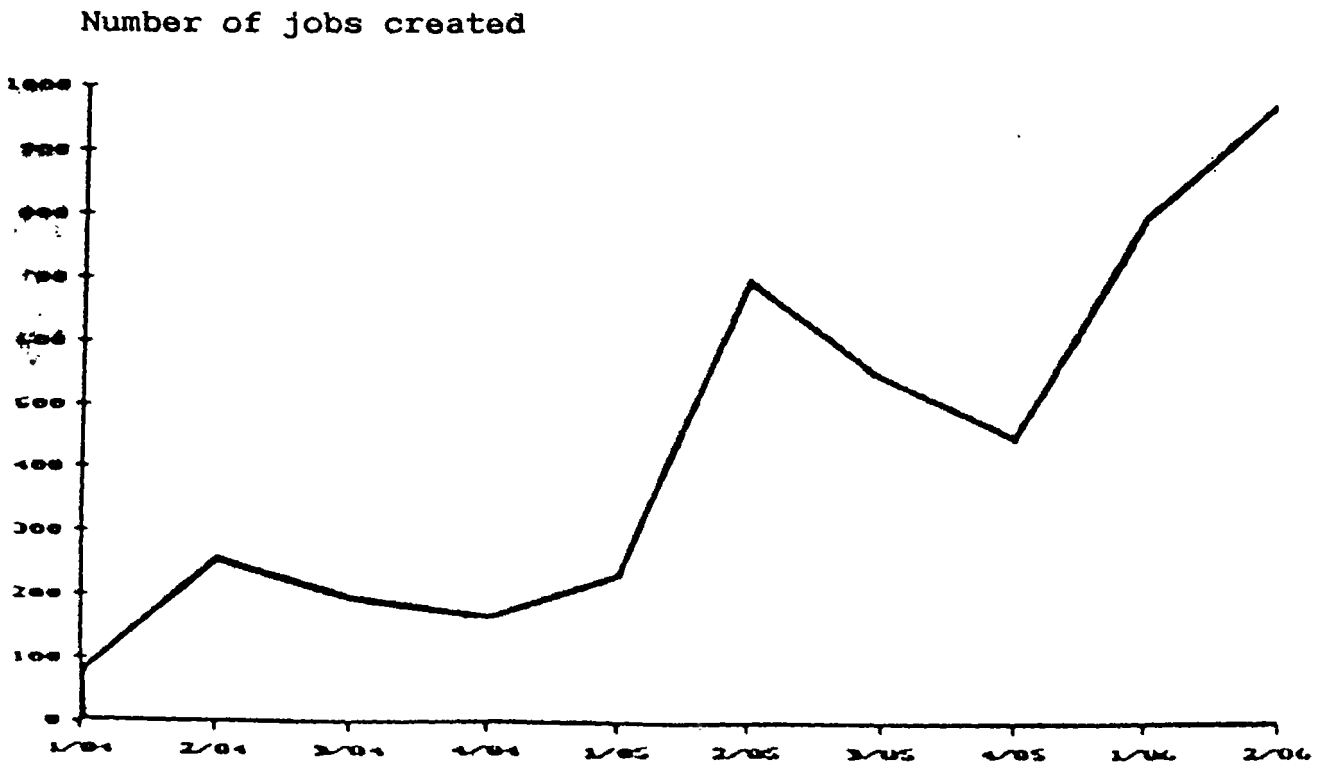
Thirdly, the organizational misfit of the implementation prerequisites and the counterproductive behaviour of the job creating units will render the programme ineffective; it will cost a lot and achieve little. Thus it will be vulnerable to criticism of the Minister of Finance that the social administration wastes money rather than making best use of it under conditions of tightening budget constraints.

It seems difficult to reject the three critical arguments against experimental programmes encouraging (a special type of) local employment initiatives out of hand. The capacity of the Austrian society to inaugurate innovations in times of adverse economic trends has not only been questioned by seasoned administrators. Hence some empirical evidence is called for. It will be provided in the next section.

"It cannot get off the ground"
(Hypothesis 1)

The programme started during the first quarter of 1984. At first it seemed to have little scope for proper development. Take-up was poor and only few provisions for handling the programme internally were made by the Labour Market Administration. But already by 12 months later it seemed to have caught on.

Chart 1
Programme development



Source: IWS Datafile AKTION 8000

Those institutions already familiar with the type of jobs to be created with the help of the "Aktion 8000" reacted fastest. They pushed on with already existing plans to expand their jobs which had been held back by financial considerations. Local communities and established non-profit-organisations (like church related welfare associations) created 80 per cent of all jobs funded by the "Aktion 8000". They showed little concern about the temporary nature of the job subsidy; they seem to be used to getting something started provided that an initial endowment is available. Long-term financial considerations do not enter their decisions as a binding constraint. Moreover they show sufficient self-confidence to face future financial pressures.

Table 1
Number of persons employed
in the period 1984 - 1986

	Number of persons employed	Per cent of Total
Province (Länder)	334	7.5
Local communities (Gemeinden)	1713	38.3
Private Associations (Vereine)	721	16.1
Other non-profit organisations (Church etc.)	1705	38.1
Total	4473	100.0

Source: IWS Datafile AKTION 8000

**"The behaviour of job creating institutions
is counterproductive" (Hypothesis 2)**

The fact that a programme has caught on does not necessarily prove it to be productive in achieving the aims set. In this context, two doubts tend to be raised:

- either that a conversion of proper jobs into "experimental" ones takes place;
- or that the incumbents of such experimental jobs get no chance to exercise relevant work skill, let alone to acquire new ones.

The "conversion" argument is not borne out by available data on the behaviour of the job creating institutions funded by the "Aktion 8000". Roughly one-third of all "experimental" jobs are transformed into permanent ones, i.e., the job creating institution keeps the person on its payroll after the funding of the labour market agency has come to an end. Only one-fifth of all jobs are merely transitory.

Even stronger evidence against the "conversion" hypothesis is the structure of wages paid for experimental jobs. Whereas in the early stages of the "Aktion 8000" the pay scales were substantially below standard rates, they seem to converge towards the union level the longer the programme lasts. In this sense, very little undercutting of going wage rates can take place in jobs created through the "Aktion 8000". At least, it

is fair to say that the readjustment of pay scales for experimental jobs does not exhibit a downward bias stronger than the one to be observed on regular Austrian regional labour markets since the 1980s.

Table 2
Post programme
career patterns

	absolute	in percent of total
Continuation of the job with the previous employer	753	30.8
Job with a new employer	468	19.1
Retraining	25	1.0
Unemployed (eligible for benefits)	515	21.1
Unemployed (not eligible for benefits)	195	8.0
Other	488	20.0
Total	2444	100.0

Source: IWS Datafile AKTION 8000

The substantial share of persons who are kept on by their employer beyond the public funding of the job indicates that the job creating institutions do not take a purely short-term opportunistic view of the services rendered by the employees.

Table 3
Areas of work

Area of work	Numbers of employed persons	per cent of total
Environmental protection	464	10.4
Social welfare services	1544	34.5
Urban and village renewal	697	15.6
Cultural activities	209	4.7
Others	1547	34.6
Total	4461	100.0

Source: IWS Datafile AKTION 8000

An additional success is evident in the fact that about one-half of the previously unemployed persons can hold on to employment after they have gone through the programme.

This group obviously had a chance to enhance (or at least stabilize) their general capacity to perform at a job. Some of the incumbents certainly get an opportunity to acquire specific skills through "learning by doing". About one-third of the jobs are located in the area of social welfare services and about one quarter in the field of urban renewal and environmental protection. Only one in six of the unemployed had to accept a job with lower skill requirements than was necessary at the person's previous job.

Thus the "conversion" argument and the "exploitation" hypothesis have to be rejected on empirical grounds. It seems that the job creating institutions do not exhibit a behaviour which in most cases could be labelled as counterproductive from the point of view of the labour market agency.

**"The experimental programme does not
meet the criteria of cost effectiveness"**

(Hypothesis 3)

Such an argument carries much weight in periods of tight budget constraints. But it is misdirected. If a specific experimental programme does not prove to be cost effective, this does not imply that experimentation is not worthwhile. Since learning through experience will always include "failures", their occurrence does not prove the futility of the overall search for new options.

Moreover, in the case of the "Aktion 8000", the experimental programme turns out to meet very high standards of efficiency: First, it is effective in the sense that, in comparison to standard measures of active labour market policies, it scores high in the dimensions of "targeting" and of "long-term employment stabilization". Secondly the net financial burden to the federal and local budgets is very low. In fact there is a positive financial return to the public purse for about two-thirds of the jobs and persons covered by the "Aktion 8000".

- (A) Together, the income generated through taxes and
- (B) the outlays (for social security benefits) saved through job creation (within the "Aktion 8000" context) add up to a larger total than the direct costs of funding and administering the programme.

This positive balance works out within the timespan of two financial years, which is well within the planning horizon of even a strongly risk-averse decision maker.

The result of such a calculation hardly comes as a surprise to anyone familiar with the high costs of unemployment in a welfare state. Nevertheless it is worthwhile to state explicitly that the "inefficiency"-hypothesis has to be rejected on empirical grounds. Experimental job creation with the help of local employment initiatives is highly cost effective.

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