

Competitive and sustainable growth: logic and inconsistency

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ABSTRACT The European Union is pursuing a competitive and sustainable development model that combines insights from environmental as well as economic analysis. The rhetoric of this model is attractive: European development should be 'sustainable' both in terms of its use of labour and environmental resources, and in terms of the location of economic activity. European policy, therefore, should encourage industries to use more labour and fewer resources, as well as to create jobs at the local level in order to internalize market externalities. Despite the appeal of such rhetoric, the implementation of this new development model poses both analytical and distributional concerns: the assumptions of environmental and economic analysis come into theoretical contradiction and the economic effects of the policy are socially undesirable. The solution is to abandon the competitive and sustainable development model, and to pursue competitive growth and sustainable resource use as separate policy objectives.

KEY WORDS Development; environment; growth; social model; unemployment; wages.

The European Union's (EU's) new Fifth Framework Programme allocates almost £3 billion [t]o support research activities contributing to competitiveness and sustainability, particularly where these two objectives interact.² Many of these activities relate to the development of new materials and the promotion of environmentally friendly practices. However, the broader intellectual roots of the project lie in the belief that economic and environmental policies can and should be integrated. This belief was recently incorporated into the foundational documents of the EU. At the June 1997 Amsterdam summit,³ representatives of the member states amended the objectives of the EU to include 'a high level of employment' and to emphasize the importance of a 'balanced and sustainable development'.⁴ They made a similar change to the 'Treaty Establishing the European Community'. In that document, the commitment to 'a high level of employment' already existed and yet member state representatives added 'sustainable' to 'development' and introduced 'competitiveness' as an objective in its own right.⁵

The purpose of this article is to examine Europe's broad strategy to achieve 'competitive and sustainable growth' and to map its implications. The argument is that the integration of economic and environmental policies is rhetorically persuasive but analytically flawed. Worse, attempts to pursue 'competitive and sustainable

growth' are likely to have important negative distributional consequences. This argument is made in five sections. The first explains the evolution of 'competitive and sustainable growth' from European Commission President Jacques Delors' proposal of a 'new development model' during the 1990s. The second focuses on implicit assumptions about factor cost and factor productivity. The third examines the dynamic relationship between the European development model and the European social model. The fourth speculates as to why the new development model could have such a powerful impact on European thinking about macroeconomics and environmental protection. The fifth projects how Europe's development model will function within an economic and monetary union and offers some suggestions for reform.

COMPETITIVE AND SUSTAINABLE GROWTH: EUROPE'S NEW DEVELOPMENT MODEL?

Talk of a European development model has emerged periodically since the early 1970s (CEC 1972). Nevertheless, the notion of a 'development model' *per se* has never achieved wide usage. Part of the explanation is that consideration of Europe's development model usually gets submerged in strong presumptions about the European social model. In this way, any attempt to assert the distinctiveness of European development runs afoul of the obvious differences between social welfare regimes. Likewise, any attempt to push for a new development model stimulates opposition to welfare state reform.

However, while Europe's development model and social model are dynamically interrelated, they can be treated as analytically distinct. In ideal typical terms, a development model describes how Europe grows or progresses to provide greater material wealth or a higher quality of life. Development is concerned with production, or the process through which wealth or quality is generated through the transformation of inputs (factors) into outputs (products). By contrast a social model describes how Europe treats the wealth (or quality of life) once it is generated. It is concerned more with distribution than with production – with who contributes and who receives rather than with how inputs are transformed into outputs. Following the logic of this dichotomy, Henry Ford promoted a development model while William Beveridge advocated a social model. Mass production and universal welfare benefits may be related, but they are not the same.⁶

Ford's paradigm for mass production lies at the heart of the 'old' development model – one that centred on volumes of output and material notions of wealth, and that tended to ignore non-market factors such as environmental degradation and quality of life. In contrast to this materialist focus, European Commission President Jacques Delors introduced the notion of a 'new model of development' at the June 1993 European Council summit in Copenhagen. Specifically, he argued that European development should change to centre around three propositions: environmental protection creates jobs; taxes on natural resources can replace taxes on labour, thereby enhancing the competitiveness of industry; and productivity growth 'must be used to improve the quality of life and create new jobs'.⁷ Delors

developed the logic behind these propositions in the Commission White Paper entitled *Growth, Competitiveness, Employment* (CEC 1993: 145–6). In abbreviated form, the argument is that:

- labour resources are under-used, while environmental resources are over-used;
- the replacement of labour with capital has reached a critical point at which the increase in labour productivity no longer justifies the ‘over-exploitation of environmental resources’; meanwhile,
- the costs of labour under-utilization (via unemployment benefits) are being added to the relative price of labour (through social security contributions) thereby ‘intensifying the tendency toward labour saving’ and leading to ‘a considerable loss in competitiveness on external markets’; and,
- the costs of environmental over-exploitation ‘represent significant but hidden welfare losses’ in that they impact on the quality of life at the local level rather than on the profitability of industry at the sectoral level.

Therefore, to be successful, Europe’s new development model has to function without this vicious cycle of inefficiency, exploitation and degradation.

The solution posited in the Commission White Paper is simple enough: clean technology and localized job creation. Because it is ‘clean’, the new technology would allow Europe’s economies to ‘decouple future economic prosperity from environmental pollution’ (CEC 1993: 147). And because jobs would be local, the quality-of-life effects of economic activity could be internalized within the community. Of course, critics will immediately point out that the only element missing from this notion of clean technology and localized job creation as the twin solutions to Europe’s environmental and employment problems is the phrase ‘by definition’. And they would be right. However, hidden within the tautology is a strong assumption that gives Delors’ rhetoric about a new development model its force: technology and location are policy variables, albeit indirect ones. In other words, the argument hinges on the belief that technological change and the location of economic activity are both somehow endogenous, that government policy can determine the ratio of inputs used in industrial processes through the manipulation of relative prices, and that market externalities can be internalized on a geographic basis: more labour, less environment; more here, less there. In the language of the White Paper:

Although economic models tend to see technological achievements as exogenous, it should be recognized that these are essentially the result of fundamental incentives originating from the public and private sectors . . . [Therefore] existing policy instruments will have to be reoriented in so far as they encourage the inefficient use of resources . . . [and] market prices will have to internalize systematically all the external costs that they generate to society.

(CEC 1993: 147–8)

The assumption that technology and location are policy variables is the distinguishing feature of Delors’ new development model. It is also the most powerful

legacy of the White Paper. Although many of Delors' specific policy recommendations were not implemented and the rhetorical usage of the term 'new development model' disappeared, the assumption that technology and location can be treated as policy variables has had a lasting impact on the European approach to the jobs crisis. The December 1993 Brussels European Council argued that workers should use 'wage moderation' to 'allocate part of productivity gains on a priority basis to investment and job creation' and recommended that the member states pay particular attention to, among other things, 'targeted reductions in the indirect cost of labour . . . in order to achieve a better balance between the costs of various factors of production'.⁸ At Corfu, the following June, the European Council reiterated the importance of reducing labour costs and went further to insist that 'increases in productivity for the rest of the century should be dedicated primarily to investments and jobs.' Moreover, the Council insisted that 'local development initiatives . . . are an essential element of the new model of development.'⁹

The culmination of this new development model came at the Essen summit of December 1994. There, the Council outlined the five areas that European policy-makers must consider when tackling the jobs crisis. Three of these concerned the quality and mobility of labour: vocational training; labour-market policies; and highly vulnerable groups such as the young, the elderly, women, and the long-term unemployed. The other two dealt with technology and location: 'increasing the employment-intensiveness of growth' through wage moderation and the reduction of 'non-wage labour costs extensively enough to ensure that there is a noticeable effect on decisions concerning the taking on of employees', and local job creation initiatives 'which take account of new requirements, e.g. in the environmental and social-services spheres'.¹⁰

The Essen formulation – and specifically the emphasis on holding down relative labour costs and on encouraging localized job creation – was reiterated at the European Council summits in Cannes (June 1995) and Madrid (December 1995). Along the way, the social component of the new development model expanded to include significant new actors. The reason is simply that changing relative labour costs in order to influence the direction of technological innovation requires the involvement of the social partners, meaning representatives of industry and labour. This is not the case when wage restraint serves only to hold down inflation or government spending, and so can rely only on action in the public sector. For example, the December 1992 Edinburgh summit, meeting before Delors posited his new development model, was satisfied to call for governments to 'make efforts to achieve restraint in wage settlements within the public sector'.¹¹ By contrast, the December 1995 Madrid summit urged the member states to continue 'the current wage restraint by linking it to productivity, as an essential element in promoting the extensive use of manpower' and yet '[recalled] that such action falls within the social partners' own sphere'.¹²

Through the record of Council presidency conclusions, it is also possible to chart how Europe's new development model has adapted to the possible contradiction between the instruments for environmental policy and the achievement of economic objectives. Any attempt to internalize market externalities at the local level –

whether directly through the imposition of tough environmental legislation or indirectly through increases in public services that result in higher taxes – risks driving away firms and jobs. The only alternatives are to apply the same standards across the market or to transfer resources from places where the externalities are positive to those where they are negative. However, common standards would need to go beyond the least common-denominator approach that is the hallmark of EU environmental policy and additional transfers would strain the resources of the Union. Simply, neither alternative would be acceptable to the member states.

The 1996 ‘European Pact of Confidence for Employment’ squares the circle for the new development model by emphasizing the role of the social partners in the enforcement of wage moderation and the importance of pre-existing European structural funds to employment promotion in some of Europe’s most depressed regions.¹³ With its adoption, the Council summits shifted their emphasis from the need for generalized wage moderation to more blanket assertions about the responsibilities of the social partners. Similarly, the Council submerged discussion of localized job creation within broader concerns for structural reform. The recommendations made by the ‘Extraordinary European Council Meeting on Employment’ in Luxembourg (November 1997) are instructive on both counts. Paragraph 18 suggests that ‘the social partners at all levels will be involved in all stages of this approach and will have their contribution to make to the implementation of the “guidelines”. That contribution will be regularly assessed.’ Meanwhile paragraph 34 contends that ‘the European Council hopes that the forthcoming reform of the Structural Funds will . . . make optimum use of the Funds to serve employment needs wherever possible in the framework of the objectives assigned to them.’¹⁴

The Confidence Pact changed the ‘implementation’ of Europe’s strategy to tackle the jobs crisis; however, the foundational assumptions of the new development model remained the same: technological innovation can be influenced by policy efforts to change the relative price of inputs and market externalities can be internalized at a local level.¹⁵ Paragraph 67 of the Luxembourg conclusions reintroduces the notion of trading off non-wage labour costs for environmental taxes and paragraph 65 emphasizes the need ‘to exploit fully the possibilities offered by job creation at local level in the social economy and in new activities linked to needs not yet satisfied by the market’.¹⁶ The new development model lurks beneath the surface of Europe’s drive for competitive and sustainable growth, and so it is relevant to consider to what effect.

FACTOR COST AND FACTOR PRODUCTIVITY

The effects of Europe’s development model play out initially in the realm of ideas. For example, as mentioned earlier, the model assumes that technology and location are policy variables. Thus one impact of the development model is to influence Europe’s policy-makers into thinking about the jobs crisis in *technological* and *local* terms. In a more general sense, the development model encourages policy-makers to think about the jobs crisis in much the same way that they think about the environment. The under-utilization of labour resources is just as egregious and

harmful as the over-utilization of environmental resources. Finally, the model suggests that policy-makers can treat economic policy and environmental policy in an *integrated* fashion. Environmental protection means jobs, and employment growth should not come at the expense of the environment.¹⁷

Such ideational influences are either superficial or normative. They tell us where to look and they suggest what should be happening. However, they do not explain why things happen as they do. Nor do they elaborate how policy-makers can influence European development – whether in narrow material or broader quality-of-life terms. These more explanatory elements of the new development model are hidden beneath the surface as assumptions about causal mechanisms. And it is here that the ideational influence of the new development model is most pronounced.

The causal mechanisms at the heart of the new development model derive both from economics and from environmentalism. The economic mechanism focuses on the role of relative factor costs. Consider, for example, two assertions: first, that changes in the relative cost of inputs can induce a technological change; and second, that a reduction in the relative cost of labour will attract job-creating investment. The first assertion appears in the argument that taxes on labour can be replaced with taxes on the environment. The second surfaces in general calls for wage restraint to enhance European competitiveness. Both assertions depend upon a single causal assumption – that firms make investment decisions on the basis of relative factor costs. At a deeper level, the assumption is that firms respond in a predictable fashion to changes in relative factor costs, either by changing technology or by changing the location for production. Without this strong assumption, policy-makers would not be able to create jobs, protect the environment, or attract investment by manipulating wages and taxes.

This assumption about the importance of relative factor costs is not without shortcomings. To begin with, there is substantial empirical evidence suggesting that firms do not act predictably to changes in relative factor costs when making investment decisions. During the period of rapid energy price rises of the 1970s and early 1980s, for example, investment patterns shifted to increase energy efficiency (that is, the productivity of natural resource inputs) but with ambiguous effects on the productivity of labour and capital. In other words, a dramatic rise in the relative price of energy inputs did have a substitution effect, but the direction of substitution was unpredictable.

Moreover, the dramatic nature of the energy price rise should not be underestimated. Smaller relative price changes are unlikely to force a strong substitution. For example, the experience of prolonged wage moderation in countries such as Belgium and the Netherlands has coincided with service sector employment growth as well as continuing labour productivity growth in manufacturing. This suggests that the change in relative factor costs had little effect on technology *per se* and instead simply moved the clearing point for the labour market down along the demand curve for labour (Jones 1999).

The explanation for this lack of predictability is that corporate executives are more likely to select investment locations and productive technologies on the basis of total factor costs (and, correspondingly, expected profits) than on the basis of

relative factor costs. This is problematic in so far as total factor costs incorporate a much broader array of factors than the stylized trichotomy of labour, capital, and natural resources. As a result, investment decisions are often sensitively dependent on initial conditions and therefore appear arbitrary to outside observers (Goodhart 1998; Krugman 1994). This means that any attempt to influence investment patterns through the manipulation of specific factor costs will work best where all other conditions can be held constant. Attempts to influence investment patterns across different initial conditions are likely to require significant changes in specific factor costs and may have dramatic and unexpected results.

The environmentalist mechanisms are numerous and focus not on factor costs, but rather on factor productivity. The underlying assumption is that productive factors such as natural resources, labour, and capital, can be substituted for each other. This assumption originates in the understanding of development as the process of increasing material wealth or quality of life through the transformation of factors into products. By implication, this means that – holding the supply of labour, capital, and natural resources constant – development is achieved through total factor productivity growth rather than through changes in the relative contributions of specific factors. In other words, the creation of wealth or the promotion of a higher quality of life does not depend on the productivity of any one of the three factors – say, natural resources – *per se*. Rather, it depends on the productivity of labour, capital, and natural resources taken together.

The problem, for environmentalists, is two-fold. On the one hand, the national income identities typically used in growth accounting do not incorporate adequate measurements of the total contribution of natural resources. Thus there is no visible market incentive to increase the productivity of natural resource use (that is, resource efficiency). Rather than maximizing total factor productivity growth, investments have focused on specific factors – namely, building more productive machines for a more productive workforce. On the other hand, the supply of natural resources is not necessarily constant and may instead be decreasing. If that is the case, far from representing a ‘missed opportunity’, the failure to invest in natural resource productivity coincides with the depletion of supplies and therefore is subtracting from overall development. In failing to focus on total factor productivity, investment planners have inadvertently made us all worse off. This explains why early environmentalists made urgent calls for a revision of national accounting statistics even as they warned of the ‘limits to growth’ (Meadows *et al.* 1972).

The emphasis on total factor productivity reveals not a single causal assumption, but rather a plethora of contested causal mechanisms – each linking factors to ‘products’. Some of these ‘products’ can be measured and others cannot. For example, increased labour productivity can be measured in terms of the money value of material goods produced per hour of work. However, if more workers were engaged to produce the same amount of goods – decreasing output per hour worked – this increase in activity would at the same time ‘produce’ more satisfaction from participating in the workforce or from contributing to society. The material productivity of labour would decline, but the ‘satisfaction’ productivity of all other inputs would increase.¹⁸

Of course, the value of such job satisfaction is impossible to measure. It is also difficult to anticipate. How can anyone be sure that a job will be satisfying? Questions such as this illustrate why the causal mechanisms borrowed from environmentalism are contested. Not only do societies demonstrate different levels of labour force participation, they also *value* such differences. Despite such contestation, however, the implications are clear. Any acceptance that work satisfaction has value means that the decrease in material productivity implied by increasing labour inputs cannot represent the change in total factor productivity. Indeed, under special conditions – that is, where the satisfaction productivity of other inputs increases more than the material productivity of labour decreases – total factor productivity may increase even as the productivity of labour declines. This is the essence of the ‘small is beautiful’ argument (Schumacher 1993 [1973]). It is also the logic behind calls for more labour intensive production processes.

Europe’s new development model is hardly new in asserting either the importance of relative factor costs or the ambiguous nature of development. The assumption about relative factor costs underwrote the policy of concerted wage restraint in the 1950s and early 1960s (Edelman and Fleming 1965; Flanagan *et al.* 1983), while the assumption about total factor productivity provided the basis for the growth debates of the 1960s and early 1970s (Beckerman 1974; Heller 1972; Lecomber 1975). In the first case, lowering the cost of labour would help to promote full employment, and, in the second case, increasing energy efficiency or substituting away from natural resources would help to reconcile growth and the environment. The new development model does not originate these arguments. Rather, it brings them together within a single framework. Analytically, the model encourages the notion that the assumptions about relative factor costs and total factor productivity cohere. Rhetorically, it pools the credibility of economic and environmental expertise – borrowing from each to give to the other.

At the same time, however, the new development model combines the weaknesses of both the economic and the environmentalist arguments. On the economic side, it offers at best a cumbersome policy instrument. Decisions about the technology and location for investment are likely to be influenced only by large changes in relative factor costs and then with potentially unpredictable results. On the environmentalist side, it broadens the basis for evaluating policy success. The objectives of adopting new technology and encouraging local investment will change depending upon subjective assessments of the functioning of specific causal mechanisms linking factors to products. The new development model not only arms Europe’s policy-makers with blunt instruments, it also encourages discretionary use. In this way, pursuit of competitive and sustainable growth is likely to underscore the diversity – and not the unity – of Europe’s member states.

DEVELOPMENT AND DISTRIBUTION

The claim that Europe’s pursuit of a new development model will encourage greater diversity can be overstated. Different member states may emphasize particular aspects of development, but this is unlikely to lead them down radically different

policy directions. Indeed, the future is more likely to bring a convergence of declaratory policies than anything else. The reason is that global market forces constrain the number of viable policy options – even if only via shared perceptions of the relationship between states and markets (McNamara 1997). Developmental objectives may differ from country to country and from culture to culture. However, decision-makers tend to respond to economic interdependence by converging on a standard set of ‘possible’ or ‘effective’ policies. Thus, whether Europe’s new development model encourages greater unity of instruments than diversity of purpose remains to be seen. Either way, however, the results are unlikely to accord with the declared objectives of the policy.

At this point it is necessary to recall that while developmental issues may be analytically distinct from distributional concerns, the two are dynamically inter-related. Development is necessary for distribution to take place, and distribution can influence the path of development. In practice, this dynamic relationship poses three complications for the new development model as a formula for matching instruments and objectives: to begin with, the manipulation of relative factor costs will be easier for some member states than for others, if only for institutional reasons. Second, any influence of changes in relative factor costs on investment decisions is more likely to increase competition for investment resources within Europe than to increase European ‘competitiveness’ in world markets. Third, the distributional consequences of changes in relative factor costs are likely to undermine the medium- to long-term stability of the development model.

The institutional argument is easiest to make. Put simply, any convergence around the importance of competitive and sustainable growth is limited by the financial requirements of the welfare state and the limits to welfare state reform. The reason for this is that fiscal flows – whether in the form of taxes or expenditures – often have effects and therefore constituencies well beyond their intended policy outcome. Therefore, in general terms, even if Europe’s national policy-makers set out to pursue similar goals through the manipulation of relative factor costs, their actions will splinter across the variety of existing institutional commitments and the diverse aspirations of vested interests (Pierson 1996).

This institutional claim also applies to the willingness of economic actors to participate in the manipulation of relative factor costs. The most often-cited illustration of this point comes from Calmfors and Driffill (1988), who claim that countries with highly centralized wage-bargaining institutions are among the best able to control the growth of direct labour costs. However, the recent proliferation of neo-corporatist style wage moderation to countries such as Ireland and Portugal necessitates an extension of the argument to include cases where the social partners accept the need for co-operation (Jones *et al.* 1998; Rowthorne 1992). For this argument, what matters is not who is most able to manipulate the relative cost of factor inputs, but rather that some countries are more able than others.

The two sides of the institutional argument can be illustrated at one and the same time. During the 1980s and 1990s, the Belgian government was able to reduce payroll taxes by openly subsidizing social welfare expenditure from general coffers – but only so long as representatives of employers’ associations and trade unions

retained the right to oversee social welfare disbursements. The Dutch faced a similar dilemma but responded more subtly. Rather than subsidize unemployment directly, they shifted almost 10 per cent of the workforce from unemployment (financed by payroll taxes) to worker disability (which comes out of general coffers). Meanwhile, the Germans had no recourse to either formula. As a result, the Belgians and the Dutch have enjoyed a near continuous real depreciation of unit labour costs relative to Germany and despite solidly fixed nominal exchange rates.¹⁹

The discussion of real exchange rates suggests a second reason why the new development model may prove unsustainable – one that derives not from relations within countries, but from the interaction between them. If labour costs fall in Germany, how will that affect investment in France? What should be the French government's response? Alternatively, will Swedish investors content themselves with cleaner lakes as opposed to larger dividends? Such questions suggest the danger of downward spirals that few in Europe would name as desirable policy outcomes – and that many denounce as empirically unsubstantiated. However, my point is not to debate the evidential merits of social or environmental dumping. Rather, it is to assert that the logic of influencing the technology and location of investment by changing relative factor costs feeds directly into concerns about a competitive suppression of working conditions and environmental standards. Therefore, either changes in relative factor costs have no effect on investment decisions, or their impact on the interaction between different sets of policy-makers is undesirable. For the new development model, the dichotomy is lose-lose.

As is often the case, the truth probably lies somewhere in the excluded middle. For example, as Fitoussi *et al.* (1993: 28–9) note in their study of 'competitive disinflation' in France, the suppression of French wages increased corporate profitability but failed to spark either an investment-led boom or a competitive emulation in the rest of Europe. In other words, the effects of a change in the relative price of labour were almost purely distributional, rather than technological or locational. French reductions in relative labour costs did not create new jobs or draw in new companies. Rather, they shifted income from labour to capital, wages to profits. Whether such profits would eventually translate into new productive investment remained (in 1993) to be seen. Judging from the macroeconomic record for the 1980s and 1990s, there is no indication that an investment increase ever came about. The labour share of value added has declined, but the ratio of gross- and net-fixed capital to gross domestic product (GDP) has fallen as well (see Table 1).

Table 1 Wage distribution and investment in France, 1983–98 (per cent market GDP)

	1983	1991	1998
Adjusted wage share	66.4	59.7	57.8
Gross fixed capital formation (private)	17.2	17.8	14.3
Net fixed capital formation (private)	6.2	6.7	3.8

Source: AMECO database, European Commission, March 1998.

Such distributional consequences constitute a third set of complications for the new development model. By shifting income from one group to another, changes in relative factor costs may yield unsustainable outcomes over the medium to long term. The French example demonstrates how a reduction in direct or indirect labour costs – in wages and payroll taxes – can shift the distribution of value added from labour to capital. Over the short term, the success of such a policy will depend upon the structure of the wage bargaining regime, the willingness of the social partners to moderate wage claims, the possibilities for welfare state reform, and the reaction of other countries – all those factors described above.

Over the medium to long term, however, the sustainability of any significant redistribution of resources from labour to capital will depend upon the structural effects of the redistribution. These effects extend beyond the technology and location for investment to include a range of factors such as the structure of domestic industry and the pattern of international trade, but also the nature of labour organization and the possibilities for the welfare state. In other words, manipulation of Europe's development model can have a powerful impact on the European social model as well.

The structural implications of concerted wage restraint are particularly open to question. Whether or not national trade union representatives eventually tire of their responsibilities for holding down wages, any major redistribution of value added will cause membership levels to decline and constituent unions to rebel against central authority. The same can be said of employers' organizations as well – albeit with the proviso that defection from centralized wage norms is likely to occur only under tight labour market conditions. In either case, the result will be a period of social unrest and wage explosions to follow the period of wage restraint (Crouch 1994).

With respect to welfare state financing, it is more useful to focus on the taxation of natural resources than on concerted wage restraint. A recurrent theme of the new development model is that any revenue shortfall from the reduction in non-wage labour costs can be made up for through increased taxes on energy or other natural resources. Yet, if the purpose of taxing natural resources is to promote progressive conservation, that revenue stream is likely to be variable and, in the long run, diminishing. The whole point of raising the relative price of natural resource inputs is to provide firms with an incentive to decrease their resource consumption and thereby lower their tax burden. This means that any successes of the policy from an environmental standpoint will challenge its successes in the labour market. Either the welfare state will have to cut benefits or it will have to seek new resources from labour or from capital. Any reduction in benefits will set off a new round of distributional concerns. Meanwhile, any additional taxes on the workforce will drive up the relative cost of labour, and any additional taxes on capital will decrease the resources available for investment.

The final point in this argument about the medium- to long-term distributional consequences of the new development model concerns the balance between different sectors of industry. Simply, the combination of incentives – low labour costs and high natural resource charges – supports a broad shift from manufacturing to

services. Such a shift is broadly consistent with a movement down the demand curve for labour – same technology, more employment. Thus, the miraculous growth of Dutch employment during the late 1980s and 1990s is concentrated almost wholly within the service sector, and does not correlate with any radical change in the pattern or volume of Dutch private investment (Van Zanden 1998; Visser and Hemerijck 1997).

The shift from manufacturing to services derives not only from the logic of manipulating relative factor costs, but also from the focus on diverse measures of total factor productivity. Once economic policy is based outside of conventional notions of value added, it matters little if service sector jobs are unproductive in material terms so long as they increase the quality of life both for the newly employed and for those who benefit from their services. Hence, as mentioned previously, the European Council at Luxembourg talked of ‘job creation . . . linked to needs not yet satisfied by the market’. The traditional notion of labour productivity as measured in terms of material output per hour worked no longer plays a central role in development.

Or does it? According to the old Fordist model, one of the benefits of increased labour productivity was a virtuous cycle of higher wages, increased consumption, greater profits, more investment, and a further increase in labour productivity. Service sector employment offers no such cyclical effects. Just because more and more people offer services does not mean that they can afford to purchase such services themselves. The benefits of increased service provision are unevenly distributed. And this inequality suggests a future defined increasingly in terms of the haves and have-nots.

THE LOGIC OF LEAST RESISTANCE

The critique of Europe’s drive for competitive and sustainable growth is both strong and apparent. Thus, the obvious question is why anyone would support the new development model – with its attendant assumptions about factor costs and factor productivity, and with its manifest consequences for income distribution – in the first place. Unfortunately, the answer is not obvious. The study of policy ideas often resembles a conspiracy theory – the principal actors are only vaguely identifiable, their motivations are inferred, their understanding of the issues is unknowable, and their material interests can only be assumed.

My analysis of the adoption of Europe’s new development model is therefore only speculative. The argument is based on who might take an interest in one aspect of the model or another as well as on who might be in a position to push the model’s adoption. For example, it is possible to suggest a motive for Jacques Delors’ initial proposal that environmental and economic policies be integrated. During the spring of 1993, Delors confronted the troubled ratification of the Maastricht Treaty, the rapid rise in European unemployment, and the expanding drive for a greater liberalization of European society. Both his presentation at the June 1993 Copenhagen summit and the subsequent White Paper were attempts to reassert the importance of social solidarity to the European project. However, doing so

necessitated a popular response to neo-liberal criticism that the European economy had simply run out of steam (Ross 1995: 221–6). The new development model allowed Delors to assert that Europe's economies were simply pointed in the wrong direction. The manipulation of relative factor costs and the encouragement of localized job creation were the instruments for steering Europe back on to the right tracks – instruments that would make growth both competitive and sustainable.

If Delors had an interest in positing the new development model, other actors had an interest in adopting it. For the trade unions – and particularly for European-level trade union representatives – the new development model offered the legitimacy of a highly visible role in economic management. As noted above – and in repeated European Councils – the manipulation of relative factor costs relies on the co-operation of the social partners. Organized labour, therefore, plays a vital role. Moreover, the combination of social dialogue and local emphasis suited all levels of labour organization. Thus, where national unions may not have been impressed with European-level negotiations in the past, they would have little objection to the type of wage bargaining asserted through Delors' new development model. A similar point could be made with respect to employers' organizations as well, albeit with the caveat that employer constituencies are even less impressed with European-level negotiations than their labour counterparts.²⁰

A final group to consider is the member states themselves. It is at this level that the distributional consequences of the new development model are likely to be most pronounced, and so it is reasonable to ask why the model has had such influence. A crass explanation could be that the new development model includes something for everyone: wage restraint for neo-liberals and wage concertation for proponents of the organized market economy.²¹ A more subtle – though no less flattering – argument is simply that the heads of state and government had no real idea how to proceed in the face of Europe's mounting economic problems. They knew that something needed to be done, but not what. Therefore, Delors' proposal to draft a White Paper on the subject was easy to accept. The broad recommendations made in that paper – including the new development model – were easy to accept as well. The decision of the European Council was neither ideological nor conspiratorial. It was practical. And, as Keynes noted in his famous aphorism about 'practical men', it is at such times that ideas can be most influential.

THE WAY FORWARD

The distributional prospects for Europe's new development model paint a fairly grim picture. Unfortunately, efforts to promote an economic and monetary union (EMU) are likely to make matters worse rather than better. The reason for this is two-fold. To begin with, EMU will increase the mobility of capital within Europe both directly and by facilitating the trade in goods. This in turn will increase the influence of relative factor cost differentials in the competition between the member states. EMU will not make firms suddenly base their decisions on relative factor costs. Rather, the point is – following McNamara (1997) – that national policy-makers *believe* that manipulating relative factor costs is important to attract

investment and to encourage job creation. Given this belief, EMU will help to ensure that any change in relative factor costs within one country becomes an immediately visible political issue in all the others.²²

The second means through which EMU will exacerbate the distributional effects of Europe's new development model is through increased pressure for welfare state reform. Such pressure will exaggerate the differences between member states' abilities to manipulate relative factor costs by preventing them from making side payments to organized labour or employers' associations, and by forcing them to focus attention on the sustainability of revenue flows (as opposed to the sustainability of natural resource usage). Both effects will work to bring the medium- to long-term distributional consequences of the new development model into the short term or even the present.

These criticisms of the new development model are not meant to encourage nihilism. Europe cannot afford to ignore the environment and neither should Europeans accept perpetual unemployment rates of around 10 per cent of the workforce. Nevertheless, Europe's policy-makers need to tackle such problems without alluding to an all-encompassing model for reform. Specifically, Europe's heads of state and government should not encourage the manipulation of relative factor costs and neither should they accept an implicit trade off between job creation and increasing labour productivity. The policy instrument is inadequate and the dichotomy is unnecessary (Gordon 1995). Finally, Europe's statesmen and women should avoid integrating the rhetoric of economic and environmental policy – particularly in ways that obscure the analytic shortcomings of both issue areas. The problem with trying to kill two birds with one stone is that you so often miss both.

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NOTES

- 1 This article was originally presented at the Annual Conference of the American Political Science Association, Boston, 3–6 September 1998. I would like to thank Paul Heywood, Chris Loewald, Andrew Martin, Kathleen McNamara, and James Walsh for helpful comments and suggestions. I would also like to thank Jeremy Richardson and two anonymous referees for providing several important editorial recommendations. Any remaining errors of fact or logic are mine alone.
- 2 This statement is taken from the official web site for the programme, <http://www.cordis.lu/fp5/src/t-3.htm>. The relevant European Council decision of 25 January 1999 can be found in the *Official Journal* 64 (1999/169/EC) pp. 40–57.
- 3 Most of the official EU documents relied upon in this article, including the presidency conclusions of the Council of Ministers, were downloaded from the press release section of the EU web site: <http://europa.eu.int/rapid>. These official documents are listed in the end notes along with their reference numbers. The various treaties are cited according to article and indent. The list of references contains only conventionally published works.
- 4 The Maastricht Treaty uses the adjectives 'balanced and sustainable' to modify

'economic and social progress', while the Amsterdam Treaty appears to distinguish between progress and development. Amsterdam Treaty, Common Provisions, Article B, first indent.

- 5 Article 2.
- 6 I should emphasize that the distinction here is idealized and would probably not sit well with those analysts who regard development models and social models as inextricably intertwined. As Andrew Martin rightly pointed out in comments on this article – a commitment to full employment plays roles in both development and redistribution. In my own analysis, I treat this overlap as an element of dynamic interconnectedness between Europe's development model and its social model.
- 7 See the seventh indent to 'Entering the 21st Century: Orientations for Economic Renewal in Europe', *European Council in Copenhagen – 21–22 June 1993 – Conclusions of the Presidency*, (DOC/93/3) Brussels: Council of Ministers (22 June 1993).
- 8 See Section I, parts A and B of *European Council in Brussels – 10 and 11 December 1993: Presidency Conclusions*, (DOC/93/11) Brussels: Council of Ministers (11 December 1993).
- 9 See Section I, parts 1 and 2 of *European Council at Corfu – 24–25 June 1994: Presidency Conclusions*, (DOC/94/1) Brussels: Council of Ministers (25 June 1994).
- 10 See 'Economic Issues', *European Council – 9 and 10 December 1994 in Essen: Presidency Conclusions*, (DOC/94/4) Brussels: Council of Ministers (10 December 1994).
- 11 See 'Annex 4 to Part A: Declaration on Promoting Economic Recovery in Europe', *European Council in Edinburgh – 11 and 12 December 1992: Conclusions of the Presidency*, (DOC/92/8) Brussels: Council of Ministers (13 December 1992).
- 12 See Section I, part A, third indent of *Madrid European Council (15 and 16 December 1995): Presidency Conclusions*, (DOC/95/9) Brussels: Council of Ministers (16 December 1995).
- 13 See, for example, 'European Pact of Confidence for Employment: Commission Communication for the Florence European Council', (IP/96/474) Brussels: European Commission (5 June 1998); 'Memorandum from the President: European Pact of Confidence for Employment', Brussels: European Commission (June 1996); 'European Confidence Pact for Jobs: Progress Report', (IP/96/946) Brussels: European Commission (22 October 1998).
- 14 See *Extraordinary European Council Meeting on Employment: Luxembourg, 20 and 21 November 1997 – Presidency Conclusions*, (C/97/300) Brussels: Council of Ministers (22 November 1998).
- 15 The term 'implementation' is placed in quotation marks because European Commission President Jacques Santer's stated objective in proposing the Employment Pact was to change the implementation of the Essen strategy for employment creation. See 'European Pact of Confidence for Employment: Commission Communication for the Florence European Council', (IP/96/474) Brussels: European Commission (5 June 1998).
- 16 See *Extraordinary European Council Meeting on Employment: Luxembourg, 20 and 21 November 1997 – Presidency Conclusions*, (C/97/300) Brussels: Council of Ministers (22 November 1998).
- 17 The theme of policy 'integration' comes up repeatedly as a priority in discussions with people working at the Commission, particularly those working at the boundaries between environmental policy and industrial policy.
- 18 By assumption, the 'satisfaction' productivity of labour is held constant. Each hour on the job is just as satisfying for the new workers as it was and is for the old workers. This assumption is necessary to exclude consideration of separate causal arguments about the satisfaction produced by working alone or in groups as well as about the amount of satisfaction and the volume of output produced.
- 19 Both the Belgian and Dutch cases are analysed in Jones *et al.* (1998). Critics of this argument will note that much of the relative depreciation in relative unit labour costs

shows up in hourly wages as well. This suggests that Belgian and Dutch efforts at concerted wage moderation are superior to those in Germany – whatever the results of efforts to reduce non-wage labour costs. However, rather than vitiate the present point about institutional commitments, the comparison of hourly wages reinforces the point about the influence of different wage bargaining regimes.

- 20 For an excellent overview of relations between national and European unions, see Branch (1998).
- 21 This is a reverse of the argument made about cohesion policy by Liesbet Hooghe (1998).
- 22 Indeed, the firms are more than eager to encourage this belief by lobbying governments to help restrain nominal wage bargains. The explicit threat is that a failure to hold down relative labour costs will force the firm to relocate. The reality, as suggested above, is far more complicated than firms would have policy-makers believe.

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