This article considers the question of how monetary union in the EU is likely to impact the preferences of governments, employers, and unions regarding the organization of wage bargaining. European Monetary Union involves a decentralization of wage bargaining (centered at the national level) in relation to monetary policy (centralized at the European level). Drawing on recent literature and on the experience of two member states (Italy and Spain), which, prior to EMU, underwent periods of intense bargaining fragmentation, the author argues that the imposition of restrictive monetary policy in a fragmented wage bargaining context in which workers nonetheless have substantial bargaining rights tends to have perverse effects. These effects ultimately led governments and bargaining actors in Italy and Spain to seek a reorganization of bargaining that gave national actors greater control over wage setting. The article considers to what extent a similar dynamic might play out in the Euro zone.

MONETARY UNION AND WAGE BARGAINING INSTITUTIONS IN THE EU

Extrapolating From Some Member State Experiences

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One of the insights of the recent literature on "varieties of capitalism" is that the economic effects of particular regulatory institutions are contingent on the broader institutional context in which they operate. This observation raises the question of how monetary union (a change in the institutional locus of monetary policy) is likely to affect other aspects of economic and social governance in the European Union (EU). By shifting monetary policy from the national to the supranational level, European Monetary Union (EMU) alters the relationship between monetary policy and other elements of economic regulation that have undergone no similar centralization.

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Key among these is the structure of collective bargaining over wages in Europe. A significant body of work by political scientists and economists suggests that the effects of monetary policy depend on the nature of the wage bargaining process on which monetary policy impinges. This means that the economic performance of the EU under EMU may come to depend strongly on the character of wage bargaining in the Euro zone. However, wage bargaining institutions themselves have been the subject of considerable change in Europe over the past decades, and the question that the literature on monetary and bargaining institutions so far has not addressed is how monetary union itself may affect the evolution of these institutions.

This article considers the question of how wage bargaining institutions in the Euro zone are likely to evolve in the new institutional context of EMU. Because the literature on monetary and wage bargaining institutions has focused on the effects of existing institutions, rather than on their origins or causes, it does not provide a ready-made theory that would allow us to predict how change in one set of institutions (the locus of the monetary authority) is likely to affect the evolution of other institutions (wage bargaining). I propose that, nonetheless, some observations about the contingent effects of institutions made in that literature may help us to understand how the preferences of actors who shape bargaining institutions are affected by monetary union.

Although EMU does not represent a change in the type of monetary regime faced by economic actors in Europe (almost all participating member states had adopted a nonaccommodating policy and independent central banks statutes well before the onset of EMU), it does involve a dramatic disjuncture between the level at which monetary policy is set and the level at which most collective bargaining over wages takes place in the EU (the national and subnational levels). By centralizing monetary policy without any corresponding centralization of wage bargaining, monetary union has produced a sharp decentralization of wage bargaining in relation to the setting of monetary policy. As the existing literature suggests, a restrictive monetary stance of the type that the European Central Bank (ECB) is committed to pursuing may have different effects in the fragmented bargaining context of the Euro zone than it did when monetary policy—albeit constrained by the European Exchange Rate Mechanism (ERM)—was adjusted at the level of the individual member states. Bargaining fragmentation means that unions may have different incentives in responding to a restrictive monetary policy than they did when interest rates were set nationally. This is likely to make monetary policy less effective and may force the ECB into a tighter stance than might have been possible when monetary policy was adjusted nationally. To the extent that such developments are recognized, I suggest that they are likely to produce shifts in the preferences of bargaining actors (employers in particular but also governments and national union leaders) in favor of bargaining arrangements that allow for greater coordination between wage setters and the new monetary authority in the Euro zone.

To illustrate my argument I focus on the experiences of two EU member states (Italy and Spain) that during the mid- to late 1980s and early 1990s underwent the functional equivalent of the decentralization of wage bargaining in relation to monetary policy that EMU entails for the EU at large—namely, a significant decentralization of wage bargaining in an unchanged national monetary policy context. The Italian and Spanish experiences may be seen as microcosmic examples of how the effectiveness of monetary policy is affected by a process of bargaining fragmentation and of how this experience in turn can affect the preferences of key actors as regards the structure of wage bargaining. In both countries, attempts by national authorities to impose wage restraint in a fragmented bargaining context had perverse effects, producing sheltered sector leadership in wage setting, persistent inflation, and real currency appreciation. This experience led to a shift in employer preferences from bargaining decentralization toward a reorganization of bargaining that aimed to reestablish the influence of national actors over wage setting and greater coordination across bargaining levels and sectors.

The first section of this article sets out the problem of the relationship between collective bargaining and the move to monetary union in the EU. In the second and third sections, I review the Italian and Spanish experiences, which involve a recentralization of bargaining at the national sectoral level coupled with (in the Italian case) cross-sectoral framework bargaining at the center after a period of bargaining decentralization. I explain the changing preferences of bargaining actors (employers in particular) by highlighting the effects that activist monetary policies had on wages in the context of bargaining fragmentation. In the fourth section, I focus on the lessons that may be drawn from the two Southern European cases for the future evolution of collective bargaining in the EU. The Italian and Spanish trajectory, I suggest, may offer a preview of how the preferences of employers (as well as those of governments and unions) may respond to the disruptive effects of EMU on wage bargaining in the EU at large. However, although these national experiences lead us to expect change in the preferences of bargaining actors in favor of some form of bargaining consolidation (or coordination), they also suggest that any such process of consolidation faces great obstacles in moving beyond the national level. They do not, therefore, tell us at what level (the national, regional, or supranational level) attempts to coordinate (and possibly consolidate) bargaining in the Euro zone are likely to take place. I conclude that, given current obstacles to EU-level wage bargaining, the most likely response to EMU in fact may be a consolidation of bargaining at the national and national sectoral levels, rather than either a radical decentralization of bargaining across the EU or an effective shift to EU-level bargaining. Last, I consider whether such nationally centered bargaining can produce sufficient coordination among bargaining actors in the Euro zone to prevent the negative interaction between wage setting and monetary policy observed during periods of bargaining fragmentation in the national cases.

EMU AND THE PROBLEM OF WAGE BARGAINING STRUCTURE

As a number of authors have noted, the move toward monetary union was driven largely by political, rather than economic, considerations on the part of EU governments (Boyer, 1998; Obsfeld, 1997). Nonetheless, public acceptance of the project has rested on the notion that EMU will have a positive impact on the future economic performance of the EU. Two kinds of arguments are typically offered to justify monetary union in this sense. The first is that EMU will boost investment and growth (and by implication, employment) by eliminating transaction costs and creating greater transparency in prices, thus promoting the further integration of markets. The second argument involves the notion that the shift to a single monetary authority modeled on the German Bundesbank will allow for an extension of the German model of macroeconomic governance—and of the outcomes historically associated with that model (low inflation, real wage moderation, and (until the early 1990s) low unemployment)—to the EU as a whole (see Waigel, 1998). In this sense, EMU was also meant to improve on the ERM of the European monetary system, which had proven increasingly untenable due to increased cross-border capital flows.

The second of these premises for EMU—that it will extend the benefits of the German model of macroeconomic governance to the EU as a whole—stands on highly shaky ground. A body of work by sociologists, political scientists, and economists suggests that the benign effects of the German model of macroeconomic governance—centering on a highly independent and nonaccommodating central bank—depended on other features of the national institutional context in which the German central bank operated. Chief among these were two features of the German collective bargaining system: the high degree of coordination among employers and among unions in the wage bargaining process (Hall, 1994) and, related to though analytically distinct from the first, the leadership of export industry in that process

(Streeck, 1994). A number of studies have also found support for these observations about the contingent effects of monetary policy in pooled time-series data for Organization for Economic Cooperation and Development (OECD) countries. Soskice and Iversen (2000), for example, find that a nonaccommodating monetary policy stance such as that pursued by the Bundesbank is capable of inducing real wage moderation (and hence a lower equilibrium rate of unemployment) only in countries with a limited (and presumably coordinated) number of wage setters. And, based on similar data, Hall and Franzese (1998) conclude that the employment cost of a nonaccommodating monetary policy is directly (and inversely) related to measures of coordination in wage bargaining. In yet another analysis, Franzese (2001) finds that these interactive effects between levels of coordination in wage bargaining and monetary policy regimes in turn depend on the influence of exposed versus sheltered sectors in wage setting.

Neither of the two conditions identified in this work as critical in supporting the outcomes of the Bundesbank's policies in Germany (a highly coordinated bargaining structure and export sector leadership in wage setting) holds true for the bargaining universe that the ECB faces (that of the Euro zone as a whole). Although the type of monetary policy that is pursued by the ECB is not particularly different from that pursued by the Bundesbank and other national central banks prior to EMU, the structure of collective bargaining in the Euro zone is far more fragmented than that on which the national central banks operated. This constitutes an important difference from the situation prior to EMU if one takes seriously the observations of Streeck, Hall, Iversen, and others cited above. Not only does the Euro zone encompass countries with more fragmented and less coordinated systems than the German, but even the most encompassing unions in countries such as Germany now represent a far smaller fraction of the workers affected by a given interest rate hike. Unions in any one country cannot be confident that an offer of wage restraint on their part will be seconded by unions in other member states whose behavior will also affect the actions of the now single European monetary authority. In addition, with a single currency, a lesser proportion of employers and workers in the EU will be vulnerable to the threat of currency appreciation (one of the main mechanisms whereby the Bundesbank and other national central banks induced wage restraint in the past). Thus, although the character of the monetary policy that unions face may not have changed in any fundamental way,[1] the incentives they face in responding to monetary orthodoxy may be quite different.

1. Except to the extent that the ECB tries to fit its policy to an average of inflation across the area, implying a somewhat tighter policy for some and a somewhat more lax one for others.

In other words, although monetary union involves little change in the type of monetary policy, the change in the locus of monetary authority fundamentally alters the character of the wage bargaining scene vis-à-vis which monetary policy decisions are made. Before EMU, wage bargaining in the EU fit a two-level coordination game in which the Bundesbank set its policy in interaction with the bargaining decisions of German unions, and other national central banks, needing to maintain their ERM parities, adjusted their decisions to the outcomes of the German coordination game. German unions knew that their actions affected the actions of the Bundesbank, and unions in other EU member states knew that their actions affected the degree of adjustment in national monetary policy that was required to maintain the ERM commitment. In all cases, national unions could assume that their actions would be reflected in monetary policy. With EMU, by contrast, there is one monetary authority looking at a plethora of uncoordinated bargaining actors, and restraint by unions in one country may not be rewarded by more lax monetary policy because lack of restraint by unions in other countries may force the ECB to tighten its stance. Thus, although the basic disposition of the monetary authority has not changed, unions face an entirely new collective action situation in responding to the central bank's actions.

All of this suggests that EMU involves a significant disruption of established patterns of coordination between monetary policy and wage bargaining in the Euro zone. Much will thus depend on how collective bargaining actors respond to this disruption, whether they seek changes in bargaining arrangements and what form those changes take. Can we predict anything about such a process of institutional adjustment from what the literature tells us about the contingent effects of monetary and wage bargaining institutions?

It will help to stipulate first that there are at least three ways in which wage bargaining actors might respond to the disruption of established patterns of coordination in the Euro zone. The first would be to seek a further decentralization of bargaining away from the national sectoral and regional levels at which most bargaining now takes place toward the local or firm levels. This would represent a choice to abandon coordination between bargaining and monetary policy in favor of maximizing the flexibility that individual firms have in responding to market conditions. The second, diametrically opposite solution would be to raise bargaining from the national and subnational levels to the EU level. This would represent an attempt to recreate the relatively centralized (and highly coordinated) framework of bargaining in which the German Bundesbank operated, and it could be done either by coordinating bargaining at the EU sectoral level (in the expectation that one sector would take a pattern-setting role) or through some form of cross-sectoral framework bargaining at the EU level. Yet a third possible response to the disruption entailed by EMU would be for bargaining actors to focus on consolidating their bargaining systems at the national level. This might allow national actors to turn the collective bargaining process into a substitute for the lost exchange rate policy capacity through which governments in the past could sometimes restore national competitiveness.

There are two kinds of arguments that might lead us to expect a choice by bargaining actors (employers in particular) in favor of the first option: a more radical decentralization of bargaining. The first involves structural trends in financial, product, and labor markets that are often seen to favor the decentralization of bargaining quite independently of the effects of monetary union. The internationalization of financial markets and increased ease of cross-border capital flows—along with changes in production regimes, new technologies, and shifts in occupational structures from manufacturing to services—are seen by some authors to undermine the viability of centralized forms of bargaining. Capital mobility is believed to punish bargaining systems that force firms to pay wages that are out of sync with either firm- or sector-specific productivity levels. And changes in production regimes and in occupational structure, on the other hand, are seen to encourage cross-class coalitions between employers and high-skilled workers in favor of bargaining systems that allow for greater wage differentiation (Freeman & Gibbons, 1995; Iversen, 1996; Katz, 1993; Regini, 1995). If general economic pressures indeed have such unidirectional implications for bargaining arrangements, then we might well expect employers to respond to the disruption of EMU by intensifying their efforts at decentralization.

A second line of reasoning that might lead us to predict intensified efforts to decentralize bargaining in the aftermath of EMU derives from the notion of institutional complementarities. In the current political economy literature, those combinations of institutions that render the best economic outcomes as seen from a cross-national perspective are often interpreted as representing alternative institutional equilibria toward which countries are pressured to move. In the literature on wage bargaining, such alternative equilibria are typically found to lie at the extremes of some measure of "encompassingness," which may be either the degree of centralization (Calmfors & Driffil, 1988) or coordination (Soskice, 1990) in wage bargaining or the extent to which wage-bargaining actors themselves are organized in an encompassing manner (Crouch, 1985). The finding that there is an elliptical relationship between such bargaining measures and measures of economic performance (such as employment) is often taken to mean that, where a sufficient encompassingness (in either the level of negotiation or the organization of the actors) is not given, economic performance can only be improved by moving to the alternative equilibrium of a highly decentralized wage bargaining system. Because EMU implies a de facto decentralization of bargaining vis-à-vis monetary policy, actors might face pressure to revert to the default option (or equilibrium) of decentralizing bargaining more fully.

There are, however, significant problems with each of these arguments. The idea that markets are creating unambiguous pressures in favor of a decentralization of wage bargaining is contradicted by empirical evidence. The most extensive study of bargaining in OECD countries to date (OECD, 1997) found no clear trend toward decentralization over the previous decade. It recorded a far more complex pattern, with some countries (Sweden, Australia, New Zealand, and the UK) experiencing a notable decentralization, others (Italy, Norway, and Portugal) moving in the direction of more centralized or coordinated bargaining systems, and yet others experiencing little change in their bargaining regimes. Another set of studies (Wallerstein & Golden, 1997; Wallerstein, Golden, & Lange, 1997) also finds no clear trend toward decentralization in either the Nordic or Central European countries or in the OECD at large.

The "alternative equilibria" view of institutional change is problematic for different reasons. Even when using pooled time-series data, most of the variation in bargaining arrangements that these studies look at is cross-sectional. It is questionable therefore that the findings of these studies offer any real insight into the experience that bargaining actors in any particular country would have if they attempted to alter the structure of bargaining from one point on the theoretical curve to another. Second, even if we were to accept the assumption that the differences in this data between countries is equal in nature to that of variation within countries over time, we cannot be sure on what part of a theoretically hump-shaped curve of economic performance the current level of fragmentation in bargaining in the EU places us (whether it is a section of the curve in which more decentralization is associated with improved performance or whether it is the part of the curve on which it is associated with a deterioration of economic performance). Last, the argument that, given an absence of encompassing bargaining organizations, the best option for economic performance is that of bargaining decentralization also seems to be contradicted by the positive outcomes of recent national incomes policy pacts in countries with divided bargaining organizations (i.e., Ireland, Italy, and Portugal).

Indeed, there are as many reasons to think that the experience of bargaining wages in the absence of a national monetary policy will push employers and unions (as well as governments) in EU states to favor a consolidation (rather than a further decentralization) of bargaining arrangements. Two factors noted in the literature regarding the contingent effect of monetary policy and bargaining institutions might lead employers and unions down this path.

The first involves what we might term the *dis*coordination effect of monetary union. As noted, the fragmented bargaining structure faced by the ECB makes it more difficult for monetary policy to elicit the kind of positive interaction in which unions deliver wage restraint to facilitate a more lax monetary policy stance (or avert a tighter stance) because fragmentation aggravates the collective action problem faced by unions in delivering such wage restraint. The second effect involves the uneven sectoral impact of monetary policy and the effect of bargaining fragmentation on the relative influence over wage trends of exposed (as opposed to sheltered) sectors. One of the principal ways in which monetary policy can elicit union restraint in wage bargaining is through the threat of currency appreciation. The effectiveness of this threat, however, depends on the influence of exposed sector bargainers over general wage and price developments, as employers and workers in sheltered sectors are less threatened by the prospect of currency appreciation and also better able to pass on higher interest and wage costs to consumers. In the absence of an established pattern-setting system, the ability of exposed sectors to exercise influence over general wage developments is likely to be higher under more centralized (or coordinated) bargaining systems because in a fragmented bargaining setting, those sectors best able to pass on costs are free to set the pace of nominal wage growth. As Swenson (1991) has shown, this problem of controlling the inflationary impact of sheltered sectors' wage settlements was central to the establishment of centralized wage bargaining in countries such as Sweden. EMU may further aggravate this problem because it reduces the number of firms for whom currency appreciation represents a serious threat as those firms engaged primarily in intra-EU trade will be far less affected by a rise in the nominal exchange rate. The ECB may thus face increased inflationary pressures and be forced into a more restrictive stance than was expected by the architects of EMU. To the extent that these effects are recognized, governments, employers, and national union leaders may seek to recapture some of the benefit of coordination by restructuring collective bargaining so as to lessen the collective action problems faced by unions and restore the influence of exposed sectors over general wage developments.

It is early days, of course, to attempt to measure the impact of EMU on the preferences of bargaining actors. Any institutional response to the disruptive effects of monetary union will involve trial and error on the part of all actors before playing out. However, we may be able to gain some insight into the effects that EMU is likely to have by looking at the experiences of states that underwent the functional equivalent of monetary policy centralization: namely, a decentralization of bargaining in an unchanged national monetary policy context.

In what follows, I will examine the experiences of two member states (Italy and Spain) to argue that attempts by the ECB to implement wage restraint in the Euro zone's fragmented bargaining context are likely to lead employer organizations, as well as governments, to back away from efforts at bargaining decentralization and to come to favor more centralized (or at least coordinated) bargaining arrangements. It might be argued that neither Italy nor Spain are particularly representative of other (in particular, northern European) member states.[2] However, in considering the effects of EMU on wage bargaining (and in turn on the preferences of actors regarding the organization of bargaining), what matters is not the extent to which the cases being considered reflect the character of bargaining in other individual member states. It is rather the extent to which they approximate conditions and events in the Euro zone at large because it is this area that is now the theater for monetary policy.

Italy and Spain are thus chosen for two reasons. First, the two countries underwent a significant process of bargaining decentralization at the end of the 1980s just as their central banks adopted a highly nonaccommodating monetary stance. This precisely is the situation that all actors now face in the Euro zone (a nonaccommodating monetary authority responding, not as the Bundesbank did in Germany to a highly coordinated set of wage bargainers, but to a bargaining context that is newly and highly fragmented). Second, although no single member state can fully reflect the complexity of the entire Euro zone's bargaining space, Italy and Spain had two characteristics that better approximate the characteristics of this bargaining space than did other member states that also underwent significant decentralization experiments prior to EMU (notably Belgium and Ireland) (see Visser, 2001). They represent relatively large economies with significant nonexposed or sheltered sectors (features that also characterize the Euro zone as a whole). And they lacked the kind of encompassing bargaining organizations (or actors) commonly associated with successful efforts at centralized bargaining—yet another feature that characterizes the Euro zone at large (although not necessarily conditions within other member states). The Italian and Spanish experiences thus may be looked at as microcosmic examples of the dynamics that follow from attempts to impose monetary rigor in a fragmented bargaining context and of the way in which these dynamics affect the preferences of bargaining actors as regards the organization of bargaining.

2. Both countries had a history of relatively lax monetary policies and rigid labor market institutions. Yet, by the period under study (the mid-1980s through early 1990s in the Italian case and the late 1980s through mid-1990s in the Spanish), both countries had undergone significant reforms and adopted very nonaccommodating monetary policy stances. For discussion, see Pérez (1998), Russo and Veredas (2000), and Jimeno and Toharia (1994).

COLLECTIVE BARGAINING TRENDS IN ITALY AND SPAIN

Despite different political histories, the labor regimes of Italy and Spain shared three important characteristics in the postwar period: (a) a historically divided labor movement, (b) highly politicized yet not highly institutionalized industrial relations, and (c) a fragmented and multitiered structure of collective bargaining. This history of division within the labor movement, poorly institutionalized industrial relations, and fragmentation and duplication in bargaining structure was generally thought to limit the ability of labor unions to act as strategic actors in these economies (Regini, 1984), leading political economists to categorize these countries as "underorganized" economies, ill-fitted (from an institutional standpoint) to the pursuit of negotiated adjustment policies. Until the early 1990s, events seemed to bear out this prediction. In the 1970s and 1980s, both countries experienced negotiated incomes policy processes (national wage agreements linked to macroeconomic policy measures) that eventually ended in failure. In Italy, an incomes policy was pursued intermittently with wage accords in 1977 and 1983. Yet disagreement among the three labor confederations (CGIL, CISL, and UIL) brought the process to an end in 1984 (Flanagan, Soskice, & Ulman, 1983, pp. 546-556; Regini, 1984). In Spain, the early concertation experiment was more successful than in Italy in the sense that a negotiated incomes policy process was sustained for almost a decade (from 1978 to 1986), even though the Communist confederation (CCOO) refused to sign several wage pacts. Yet it too broke down in 1986, when the Unión General de Trabajadores (UGT) decided to join the Comisiones Obreras (CCOO) in a more militant stance. Several attempts by the Socialist government to reach a new wage pact thereafter failed to bring the unions back into the fold (Gillespie, 1990; Pérez, 2000; Royo, 2000).

In both countries, the collapse of these early concertation experiments was followed by a period of fragmentation and decentralization in bargaining. In Italy, many firms opted for firm-level bargaining to broaden wage differentials during the 1980s (Erickson & Ichino, 1995), disrupting the traditional pattern in which contractual minima were set at the national sectoral level and then adjusted via the *scala mobile* (an automatic wage indexation mechanism). In a number of sectors, national agreements failed to be reached, and in others, they simply followed the terms of previously negotiated local agreements (Katz, 1993; Negrelli & Santi, 1990). In Spain, the end of concertation in 1986 led bargaining to default to the underlying structure inherited from the Franco period, which, with a few exceptions, was dominated by bargaining at the provincial-sectoral level. In both cases, bargaining during this period (from 1984 to 1992 in Italy, from 1987 to 1994 in Spain) took place in a highly fragmented manner without effective coordination by either employers or unions across bargaining units.

The trajectory of Italy and Spain up until the late 1980s thus appeared to confirm the view that, given a lack of unitary labor organizations, economic pressures would force these countries down a path of bargaining decentralization similar to that followed by Britain in the 1980s. The subsequent course of events in the 1990s, however, runs against this conclusion as both countries experienced a marked reversal in the direction of institutional change with efforts to recentralize and coordinate bargaining throughout the economy. This reversal was most explicit in the Italian case, in which, by the end of the 1980s, national-level negotiations to control wages had resumed. In 1992, the unions agreed to the abolition of the *scala mobile* and to a 2-year freeze on company-level bargaining to support the government's emergency austerity program, and a year later they signed a tripartite agreement that institutionalized a new incomes policy framework that, for the first time, attributed distinct roles to different levels of bargaining. According to the new system, national sectoral bargains (which are subject to national intersectoral framework discussions) set wage increases in line with expected inflation, whereas lower-level bargains (at either the firm or locality level) determine pay scales and distribute additional productivity gains. This formalization of a two-level bargaining structure subject to an overarching incomes policy framework was reaffirmed in the 1998 "patto di Natale" with one major innovation: that national agreements would henceforth use the European (rather than Italian) inflation rate as their referent (Locke & Baccaro, 1996; Negrelli, 1998; Regini, 1997; Regini & Regalia, 1997; Rhodes, 1998).

The turn of events in the Spanish case was less drastic than in Italy. An attempt by the Partido Socialista Obrero Español (PSOE) to reach a new national wage accord ended in failure in 1994 when the government unilaterally abolished a category of regulations called "labor ordinances," leaving it up to employers to reach agreements with the unions on the thus deregulated aspects of industrial relations. In the period following the standoff over this reform, however, the industrial relations scene in Spain experienced a significant transformation. In late 1994, employers and unions signed an agreement to regulate the devolution of regulatory competencies to the collective bargaining process, defying the expectations of those (including union leaders) who had feared that the loss of the labor ordinances would produce a deregulatory spiral. And the PSOE's electoral defeat in 1996 was followed by an unprecedented series of national agreements: one in 1996 between the new conservative government and the unions, on pension reform; another in 1997 between the employers and the unions reducing dismissal costs, further agreement on pensions between the government and the unions in 2001, and finally, a new national wage accord in 2002. (Confederación Española de Organizaciones Empresariales [CEOE], 1999; Consejo Económico y Social [CES], 1996, 1998, 1999; and *El Pais*, October 29 and 30, 1998).

More important, although a new national wage accord was not reached until 2002, there has been a steady effort to recentralize and coordinate wage bargaining by other means since 1994. In 1997, the two labor confederations and employers signed a landmark agreement to lessen the degree of fragmentation in bargaining by giving a primary role to national sectoral bargains in setting overall wage guidelines. Unlike the Italian agreements, it did not mandate change, yet it reflected a process of bargaining consolidation that was already underway. Thus the proportion of workers covered by national sectoral bargains rose from 22% in 1993 to 30% in 1999 (the last year for which figures are available) (CES, 1997; Ministerio de Trabajo, 1998, 2002). There has also been some consolidation in the number of sectoral divisions around which bargaining is organized, the most significant example of which was an agreement to consolidate bargaining in the previously atomized metalworking sector (*European Industrial Relations Review*, May 1998). And although the Spanish unions long eschewed a return to formal incomes policy agreements, preferring to trade wage restraint for employment-related concessions on a sectoral basis, there is substantial evidence that they began instrumenting an informal incomes policy of sorts starting in 1994 (Pérez, 2000). The most striking manifestation of this is the remarkable wage moderation sustained through years of record employment growth at the end of the 1990s.

EXPLAINING THE INSTITUTIONAL REVERSAL

The moves in Italy and Spain to establish a more orderly division of labor among bargaining levels and to give a central role to national sectoral agreements constitute efforts to establish the institutional bases for greater coordination in wage bargaining. These efforts, following a period in which bargaining had been allowed to take place in a decentralized manner, are particularly striking because they occurred at a time when both countries faced a sharp intensification of European and international financial market integration. Given the widespread notion that financial integration favors a deregulation of labor markets, how are we to explain this reversal in the course of institutional change in Italy and Spain?

Two possible answers may be deduced from the analyses of scholars who have focused on the related, yet more general, phenomenon of the resurgence of "social pacts" in Europe. The first is that the resort to national bargains on wages and other issues during the 1990s was simply a function of the efforts by governments and employers to secure their country's participation in monetary union. Faced with the deadline to meet EMU convergence criteria, so goes this view, authorities in Italy and Spain (as well as other EU states) sought agreement with the unions as a way to break persisting standoffs over pensions and labor market reforms. The implication is that such efforts constituted temporary quick fixes and that developments in the long term are likely to bear out the conventional prediction of a return to a more deregulatory path. The second argument sees more persistent causes behind the wave of social pacts in the 1990s and relates to the role of social consensus within firms in sustaining competitiveness. Marino Regini, for instance, has argued that increased international competition at the end of the 1980s and 1990s heightened the importance for employers of controlling costs rather than just improving flexibility and that this led to government-brokered incomes policy deals of 1992 and 1993 in Italy (Regini, 1995, 1997; Regini & Regalia, 1997). Unlike the political exchanges of the past, he suggests, the new social pacts are an institutional mechanism to boost international competitiveness through consultative practices that generate social consensus. Along similar lines, Martin Rhodes (1998) has argued that the new corporatism exemplified by Italy was made necessary by the conflict between two countervailing economic pressures on firms: the need to control costs, which induces employers to seek external labor market flexibility (i.e., flexibility in hiring practices) and the need for cooperative relations within firms, which are easily undermined by excessive external flexibility. The new "competitive" corporatism in Europe, Rhodes suggests, reflects an attempt by employers to reconcile these two needs (limiting the reliance on external flexibility to maintain cooperative relations within firms while controlling costs).

The first view (that the search for new social bargains in Europe is just an epiphenomenon of the rush to EMU) does not seem consistent with important aspects of the developments described in the previous section. To be sure, the imperative to meet the EMU criteria gave Italian and Spanish authorities an important new motive to seek agreements with the unions in the early 1990s. This motive seems particularly relevant in explaining the decision by governments to seek global wage pacts to control inflation as well as pension pacts to control public spending. The bargaining reforms undertaken in Italy in 1992 and 1993 and those spelled out in the 1997 agreement in Spain, however, went well beyond the short-term objective of achieving an inflation target in a given year. In both countries, employers and unions placed a great deal of emphasis on institutionalizing a new bargaining structure (giving the national sectoral level a framework-setting role over wage setting at lower levels). It is unclear how the short-term objective of meeting the EMU deadline would lead employers to favor (or even agree to) such a long-term restructuring of the bargaining system.

The analyses of Regini (1995, 1997) and Rhodes (1998), on the other hand, explain the lack of support for a British-styled deregulation of labor markets in Italy and Spain. Controlling costs by limiting employment protection and dismantling consultative mechanisms may not be worth losing the cooperative climate within firms that allows these to adjust production practices and compete on quality rather than price. Yet it is not clear how this microeconomically based explanation of the need for cooperation within firms explains the effort to coordinate wage bargaining at the national level. After all, one of the principal arguments in favor of decentralized bargaining is that it allows a closer match between wages and firm- or locality-specific conditions. Both authors suggest that the reason for the renewed interest in higher level bargaining had to do with the need to control labor costs. Yet they do not explain why employers found it so difficult to control these costs in the fragmented bargaining context of the late 1980s. To understand this, we must look at the macro dynamics in wage setting that occurred once governments attempted to impose disinflation unilaterally by way of monetary policy measures in the fragmented national bargaining contexts that characterized the two countries during the late 1980s and early 1990s.

The inability of Italian and Spanish employers to control wages once concertation in the 1980s had come to an end is reflected in the upward evolution of real wages in the two countries from the mid-1980s to the early 1990s (Figure 1). In Italy, the disinflation initiated with the incomes agreement of 1983 was sustained through 1986, and Italian authorities combined a relatively moderate monetary stance with periodic devaluations. But it ended in 1987, when wage growth accelerated, first in the public sector and thereafter in the private sector. A renewed rise in inflation led the Italian authorities to tighten their monetary stance considerably in that year and to resort to quantitative credit controls to stop capital outflows. Yet continued pressure on the lira forced devaluation in January 1990. Thereafter, Italian authorities intensified their new strategy of trying to break inflation through monetary policy measures by lifting all capital controls, shifting the lira into a narrow 2.25% ERM band, and making a firm commitment to maintain this parity through whichever monetary policy measures it took. This "strong currency" policy resulted in a significant loss of competitiveness (Figure 2) and a large widening of Italy's current account deficit from 1989 to 1992. Yet it had remarkably little impact on either wages or prices. An end to wage and price inflation was only achieved with the lira's devaluation in the 1992 ERM crisis and the incomes policy accords of 1992 and 1993. Thereafter, wage and price growth slowed drastically (Figure 1).

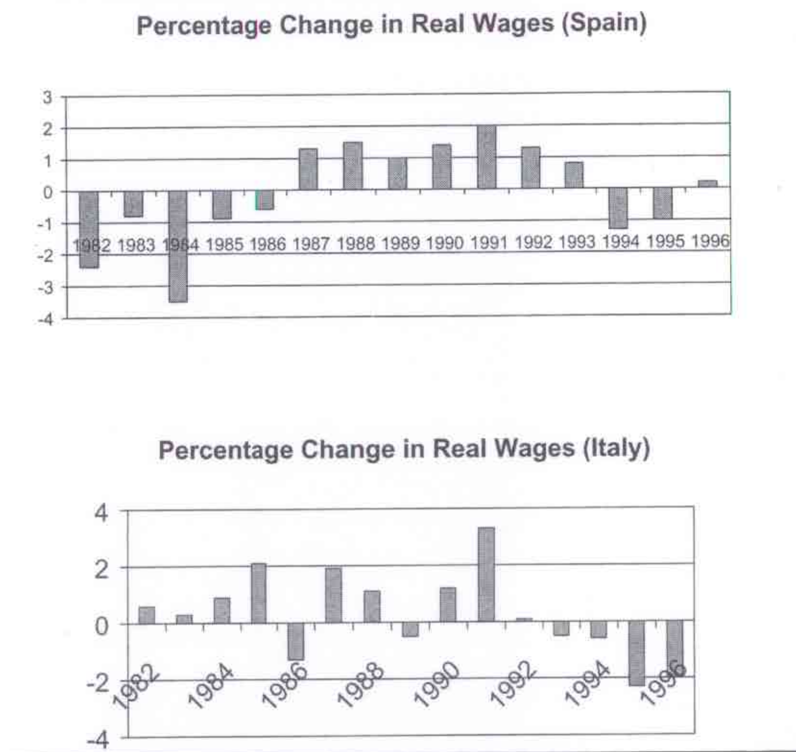

Figure 1. **Percentage change in real wages for Spain and Italy based on contractual hourly wages and consumer price index.**
Source: OECD, Economic Outlook; OECD, Main Economic Indicators.
Note: Italian wages reflect the industrial sector only. OECD = Organization for Economic Cooperation and Development.

A similar experience can be observed in the Spanish case. The inflationary surge in wages and labor costs that occurred during the initial stages of the transition to democracy was halted by the incomes policy agreements of the early 1980s, leading real contractual wages to decline for a number of years. This trend, however, came to an end in 1987, the first year not covered by a framework wage agreement. Real wage growth turned positive and remained significant through the end of the decade (Figure 1) considering the still very high levels of Spanish unemployment. And, as in Italy, this acceleration in wages occurred in the context of a very tight monetary policy. Spanish interest rates were allowed to rise to such levels at the end of the decade as to make the peseta the strongest currency (closest to its upper band) in the ERM for almost three consecutive years following its 1989 entry into the system. Yet,

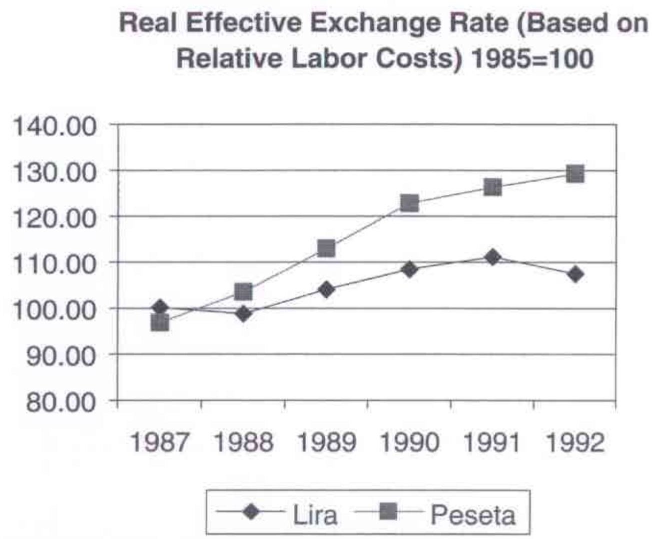

Figure 2. **Real effective exchange rate based on relative labor costs (1985 = 100).**
Source: IMF, International Financial Statistics.

as in Italy, this high interest rate/strong currency strategy was remarkably ineffective in limiting inflation. Only after the national union confederations decided to impose a new, centrally directed strategy of wage moderation (i.e., an informal incomes policy) in 1994 was this dynamic brought to an end.

This background sheds an important light on the efforts to recentralize bargaining in Italy and Spain. In both countries, governments sought to impose wage restraint in a fragmented bargaining context by making a firm exchange rate commitment and allowing real interest rates to rise to very high levels. Yet this monetary-policy-centered strategy failed in bringing about wage and price restraint, resulting in an intense loss of competitiveness (see Figure 2). How is this extended failure to impose disinflation through monetary policy to be explained?

Analyses of financial flows and wage- and price-setting trends in the two countries during this period reveal two principal causes. One of these was the changing external context of the late 1980s and early 1990s.[3] With the lifting of capital controls in the late 1980s, the combination of a fixed exchange rate commitment and a staunch monetary policy course had the effect of producing large inflows of short-term, speculative capital into Italy and Spain that sought to take advantage of the two countries' high interest rate differentials vis-à-vis other ERM countries (OECD, 1990, pp. 30-32, 1991, pp. 43-45). These capital inflows were more volatile in the Italian case than in the Spanish case because of periodic crises of confidence in Italian public finances. Yet they had roughly similar effects. They made it very difficult for monetary authorities to retain a grip on domestic liquidity levels because they created a vicious circle in which interest rate hikes intended to send a signal to domestic wage bargainers provoked a rise in short-term inflows, which in turn required further interest rate increases, which encouraged further inflows, and so on.

3. The incompatibility of an independent monetary policy, fixed exchange rates, and high capital mobility (the so-called Mundell-Fleming condition) is discussed in Frieden (1991).

The combination of capital mobility and fixed exchange rates became a significant obstacle for monetary policy authorities in Italy and Spain at the end of the 1980s. Yet it was not the only or even most important factor behind the failure of monetary policy. Equally, if not more, important was the sectoral dynamic that the policy stance adopted by Italian and Spanish authorities set off in wage and price setting once bargaining was no longer subject to any form of central coordination. The strategy pursued by the two governments was premised on the notion that higher interest rates and a strong currency would discipline wage growth by forcing employers in exposed sectors to resist higher wage demands (OECD, 1992, pp. 21, 28; Pérez, 1998). Yet this required that bargaining in exposed sectors (i.e., those sectors affected by currency appreciation and not able to pass on higher interest costs) carry significant weight in determining the pace of wage and price growth throughout the economy. In the context of a fragmented and uncoordinated bargaining structure, the heavy reliance on a tight monetary policy, however, had the opposite effect: It encouraged a shift of resources away from exposed sectors (those hardest hit by currency appreciation and least able to pass on costs) toward sheltered sectors (those least affected by currency appreciation and best able to pass on both higher wage and interest costs) (Pérez, 2000). One manifestation of this divergent impact was the growing discrepancy between consumer and producer prices over the period. From 1985 to 1992, the consumer price index for services (i.e., nontradeables) exceeded that for producer prices (i.e., tradeables) by nearly 50% in Italy and 60% in Spain, whereas the divergence between the two measures for the same 7-year period was only 10% in Germany. Divergent price trends in turn downgraded the ability of exposed-sector wage bargainers to influence the course of general wage trends. The more the authorities relied on the monetary lever, the more conditions in exposed and sheltered sectors diverged, and the more wage settlements in sheltered sectors came to determine the rate of price and nominal wage growth in the economy.

This sectoral dynamic whereby aggressive wage settlements in sheltered sectors increasingly set the standard for nominal wage growth throughout the economy was a key factor behind the paradox of persistent inflation in the face of a tight monetary stance (OECD, 1992; Raymond, 1992). In Italy, the pattern became one in which generous public sector settlements usurped the traditional role of the metalworking sector in setting the standard for other sectors. In Spain, it was private service sector settlements (in the booming financial services and construction sectors in particular) that began to set the tone of wage negotiations once the UGT stopped trying to moderate wage demands across sectors (Pérez, 2000). In both countries, governments and central bankers thus had to face the limits of a unilateral use of monetary policy to control wages in a fragmented bargaining context. And it is this realization that led them to seek a return to bargained incomes policy in the early 1990s. In Italy, Carlos Ciampi (governor of the Bank of Italy) observed as early as 1988 that monetary policy measures alone were proving insufficient to preempt excessive wage settlements and that a new incomes policy agreement would be needed to bring inflation under control. Five years later, as prime minister, he would insist on the point in his efforts to convince Confindustria to accept union demands during negotiations for the 1993 incomes policy accord ("Ciampi Sets Wage Deadline," 1993; "Italian Bankers Air Grievances," 1988). In Spain, it was a stiff warning from the IMF that an incomes policy agreement would be necessary to control inflation that led to the PSOE government's first serious effort to reach a new agreement with the unions in 1990 ("IMF in Tough Warning," 1990; "Madrid Economic Policy," 1990). In the end, of course, the effort was more successful in Italy than in Spain, where the failure of negotiations in 1993 prevented a rapid adjustment in wages and aggravated the economic crisis.

Although the failure to combat inflation explains the eagerness of governments to reestablish incomes policy accords, the experience of employers and unions in the 1987-1992 period is crucial in understanding the efforts to reform the underlying structure of collective bargaining in the two countries. Having favored decentralization in the 1980s, employers found that they were not able to impose wage restraint in a context in which high interest rates encouraged capital to flow into the most sheltered sectors of the economy and in which settlements in those sectors came to set the pace of nominal wage growth. This unintended consequence of decentralization appears to have been recognized first by employers in exposed sectors.[4] Yet the dynamic of sheltered sector leadership hurt employers in all sectors. Even if sheltered sector employers could better afford the higher wage demands they faced at the local level, they too had been better off during the period of concertation when national labor leaders had set wage guidelines. Hence, although in the case of Spain the regional employer affiliates resisted a mandatory reorganization of bargaining at the national sectoral level, there was broad consensus within both the CEOE and Confindustria that bargaining fragmentation was proving a major obstacle in wage negotiations.

The explanations offered by representatives of the national employer confederations for the 1992-1993 Italian reforms and the 1997 Spanish agreement clearly indicate the centrality of the macroeconomic dynamic described above in shifting employer preferences. Whereas prior to the decentralization experiments, employers had attributed inflationary wage settlements to institutional arrangements such as the *scala mobile* in Italy and the widespread practice of negotiated compensation clauses in Spain, it was now recognized that the dismantling of such arrangements would not suffice. As one representative of Confindustria explained, settlements in the public sector and in other sheltered sectors such as utilities would dominate wage demands in industry even in the absence of indexation as long as bargaining remained fragmented along both horizontal and vertical lines.[5] This led the confederation to seek a complete centralization of wage bargaining in the form of "a single locus of collective bargaining at the national level" during the 1993 negotiations (a proposal that was rejected by the unions who insisted on retaining a secondary role for lower bargaining units) (Locke & Baccaro, 1996, p. 299; "Survey of Italy," 1992). A representative of the Spanish employer confederation offered a similar explanation for why the CEOE accepted—and in indeed appropriated as its own—the commitment to restructure bargaining in favor of national sectoral bargains during the negotiations that led to the 1997 accord.[6] Bargaining consolidation, he explained, would increase the influence of national union leaders, who took a broader view of wage negotiations than local-level labor representatives.

By contrast to the experiences of governments and employers, that of the unions during the period was more complicated. In both Italy and Spain, the concertation processes of the 1980s came at significant cost for the national

4. In Italy, the move to recentralize bargaining was promoted within Confindustria by large manufacturing firms such as Fiat and Zanussi and the Chemical Industry Employer Federation (Baccaro, 1999). In Spain, it was the Catalan employers (Fomento de Trabajo), dominated by manufacturing firms, along with the metal sector employers (Confemetal), who led in seeking new bargaining arrangements with their regional and sectoral union organizations in the 1990s.

5. Interview with an official of Confindustria's Labor Relations Department, Rome, June 1999.

6. Interview with CEOE labor relations department officer (Madrid, May 1999). A CEOE study (1999, p. 52) showed national sectoral bargains yielding lower increases than provincial and regional bargains.

labor confederations, although this cost took different forms. In Italy, the effort to sustain concertation in 1984 brought an end to the unity of action that the unions had mustered in the aftermath of 1968. The wage compression that resulted from the 1975 *scala mobile* accord also produced widespread discontent among skilled workers and gave rise to independent unions that grew significantly in the 1980s (Locke & Baccaro, 1996). In Spain, the absence of a compression mechanism such as the *scala mobile* prevented the emergence of independent unions. Yet the concertation agreements of the 1980s hurt the UGT, which was held responsible for the decline in real wages incurred during the decade.[7] The periods of bargaining decentralization, by contrast, were periods of relatively high real wage gains in both countries.

Given the negative experiences with centralized bargaining and the relative gains achieved under decentralized bargaining, the unions' willingness to make significant regulatory concessions to reestablish a more coordinated form of bargaining in the 1990s may seem puzzling. Yet it is less so if one considers the way in which fragmented bargaining, particularly in a tight money context, also undermined the ability of national labor confederations to mediate between the interests of workers across sectors and thus to act as strategic actors in the economy.[8] In Italy, the confederal unions' ability to respond to the economic crisis of the early 1990s was challenged by the independent unions that were largely behind the large public sector increases that drove wage bargaining in 1990 and 1991. The Italian bargaining reform of 1993 thus was accompanied by a reform of plant-level representation procedures that strengthened the confederal unions at the expense of the independent unions (Baccaro, in press). In Spain, the dramatic increase in unemployment that followed the 1992 currency crisis increased the perception that the unions represented a shrinking fraction of "insiders" at the expense of the unemployed, challenging their legitimacy (Richards & García Polavieja, 1997). This led to leadership struggles within the two confederations in which union leaders who favored the aggressive use of decentralized bargaining squared off with moderates who wanted to give greater priority to employment. The victory of moderate leaders in both confederations cleared the way for the new strategy of wage moderation adopted by the unions in 1994. Once the strategy of exploiting sectoral and local advantages to achieve higher settlements had been abandoned, the effort to reconsolidate bargaining at the national sectoral level followed. Global (or cross-sectoral) wage

7. The UGT lost its dominance in plant-level elections over the period.

8. Locke and Baccaro (1996, p. 292) also point out that the *scala mobile* limited the significance of bargaining because it took up most of the room for wage negotiations. By replacing it with incomes policy and national sectoral bargaining, the confederations vastly increased their importance in the life of workers.

negotiations, however, were rejected until early 2002, when a new wage accord was reached, as both CCOO and UGT leaders felt that they could achieve greater employment-related concessions in return for wage restraint at the sectoral level.[9]

In various ways, the perverse dynamic of monetary orthodoxy in a fragmented wage bargaining context thus produced a convergence in the preferences of all actors in favor of a reconsolidation of wage bargaining. The inability of central banks to impose price restraint led public officials to seek new incomes policy agreements with the unions—a search that proved successful in Italy but only slowly so in Spain. Employers, meanwhile, had to come to terms with their inability to control labor costs in the context of an economic policy that placed far greater pressure on exposed sectors than on sheltered sectors and a bargaining structure that allowed the latter to set the pace of nominal wage growth. Meanwhile, the unions were led back to the bargaining table by their realization that bargaining fragmentation was eroding their position as economic and social actors. They then chose to give up past statutory guarantees (the *scala mobile* in Italy; high dismissal costs in Spain) in return for a devolution of authority to the bargaining process and a reassertion of the role of national confederations and national sectoral federations within that process.

THE SOUTHERN EUROPEAN EXPERIENCE AND COLLECTIVE BARGAINING UNDER EMU

In the years leading up to the 1992 ERM crisis, Spanish and Italian authorities went farther than most other EU member states in trying to impose wage restraint through high interest rates in a fragmented and uncoordinated wage bargaining context. Yet, as we have seen, these attempts misfired. Bargaining fragmentation played up the uneven sectoral impact of monetary policy, allowing those sectors best able to pass on costs to set the pace of wage growth. This in turn produced a shift in the preferences of key actors (employers in particular but also governments and unions) in favor of a reorganization of bargaining that would reestablish the influence of national organizations and allow for greater coordination in wage setting.

To what extent are these experiences relevant to understanding how monetary union may impact wage bargaining across the Euro zone and how the preferences of European bargaining actors may evolve in the future. To be sure, there are significant differences between the national examples dis-

9. Interviews with UGT and CCOO leaders, Madrid, fall 1998.

cussed and the more complex bargaining geography of the Euro zone. One of these is the multiplicity of actors and legal frameworks involved in bargaining across the Euro zone. Another is the nature of bargaining fragmentation, which in the Euro zone runs mostly along national (rather than subnational) lines. Nevertheless, there are reasons to believe that the national experiences may offer a preview of the way in which the preferences of actors involved in bargaining may be affected by monetary union.

As noted earlier, the literature on monetary policy and wage bargaining offers two reasons why monetary policy is less likely to succeed when wage bargaining is fragmented yet workers have strong bargaining rights. The first is that a central bank's attempts to signal its intentions to wage bargainers is less effective when there is a large number of players involved. The second is that bargaining fragmentation exacerbates the collective action problem faced by unions in agreeing to wage restraint. The Spanish and Italian experiences highlight a third factor that exacerbates this later collective action problem: An activist monetary policy impacts firms and sectors that are exposed to competition far more than those that are not, augmenting the disparity of conditions between the two and encouraging a shift of resources from the former to the latter. When bargaining is not subject to coordination by actors that take a comprehensive view of the economy, a restrictive monetary stance may therefore simply allow the most sheltered (and hence inflation-prone) sectors to set the pace of nominal wage growth.

All three of these problems are likely to present themselves in the Euro zone sooner or later. The multiplicity of national bargaining scenarios makes it more difficult for the ECB to establish a clear interaction between its decisions and those of bargaining actors (the signaling problem). The collective action problem faced by unions in responding to monetary policy is intensified by the fact that, individually, even the largest national unions represent only a small proportion of workers in the Euro zone (the more aggressive bargaining stance adopted by German unions starting in the spring of 1999 seems to offer some early evidence of this). This collective action problem may be mitigated to the extent that national unions engage in strategies of competitive disinflation (trying to promote domestic employment by undercutting wages in other countries). Yet, at the same time, it is likely to be exacerbated by the uneven sectoral effects of monetary policy illustrated in the national experiences of Italy and Spain. Indeed, EMU has the potential of augmenting the perverse effect that monetary policy may have on sectoral leadership in wage setting because, although it increases competition in some markets, it also renders a lesser proportion of economic activity (that engaged in intra-EU trade) subject to changes in currency valuation. This lessens one of the mechanisms (the threat of currency appreciation) through which monetary orthodoxy is thought to contribute to wage moderation.

All of this suggests that, although EU policy makers and employers have focused on rendering labor markets more flexible, they should become increasingly interested in promoting bargaining arrangements that allow for greater coordination between the ECB and wage bargainers. From a theoretical standpoint, this objective would seem to be best achieved by raising the level at which wage norms are set from the national and subnational levels to the European level, either by way of global framework bargaining or through EU-wide sectoral agreements. In the latter case, the ECB could focus its policy signals on one or two lead sectors at the European level, replicating the pattern once followed by the Bundesbank in Germany.

An upward shift in wage bargaining to the EU in some form or other is not an entirely unthinkable prospect. Led by the German metal workers federation, which wanted to preempt regime competition under EMU, the national union confederations of Germany, Belgium, the Netherlands, and Luxembourg signed an agreement in September 1998 in which they agreed to coordinate their bargaining strategies. The so-called Doorn Declaration set out a general norm to guide future wage claims: namely, that wage demands be based on the sum total of cost-of-living changes and labor productivity increases in the four countries. The Doorn Declaration was followed in December 1998 by the adoption of a "European coordination rule" by the European Metal Workers Federation. And at its 9th congress in July 1999, the European Trade Union Confederation (ETUC) called for a generalization of such cross-border, sectoral coordination in wage bargaining to produce a "European solidaristic pay policy" (European Industrial Relations Observatory [EIRO], 1998, 1999a).[10]

The idea that EMU requires a restructuring of collective bargaining in the EU has also received attention from policy makers. Starting with its 1994 European Works Council Directive, the European Commission has encouraged a process of top-level talks (or social dialogue) between the European social partners (ETUC and UNICE), producing several significant agreements (e.g., parental leave in 1996, part-time work in 1997, and fixed-term work in 1999) and leading to the establishment of 23 EU-level "sectoral dialogue" committees in 1999. It also has been publicizing (again since 1994) Broad Economic Policy Guidelines (BEPGs) that include guidelines on wage development. Last, at the 1999 Cologne summit, the European Council

10. Four other sectoral federations (private services, textiles, printing and paper, and building and woodworking) have also adopted EU-wide coordination rules but with substantial divergence in the autonomy that is left national federations.

approved an "Employment Pact," with the stated goal of achieving a "mutually supportive interaction between wage and price developments and monetary, budgetary, and fiscal policy through macroeconomic dialogue aimed at preserving a noninflationary growth dynamic" (EIRO Online, 1999a; EU Commission, 2000). The pact set off the "Macroeconomic Dialogue," a process consisting of regular meetings between representatives of ETUC, UNICE, the EU Commission, member governments, and, most important, the ECB.

However, although there has been a flurry of agreements among European labor unions and talk of macro coordination by EU policy makers, the likelihood of actual wage setting at the European level remains remote. As one survey conducted by the EIRO documents, such a move faced virtually unanimous opposition from European employers. This opposition was stated most adamantly by German and Swedish employers, who had backed decentralization of bargaining in their countries until recently. But it is also evident among employers in other member states (EIRO, 1999a).[11] Moreover, although the experiences of Italy and Spain illustrate the failure of attempts to impose wage restraint through monetary policy in a fragmented bargaining context, those same experiences also suggest that there are obstacles to any effective shift to EU-level wage bargaining going beyond the former Deutschmark zone (i.e., Germany and the Benelux countries). The most important such obstacle is the near impossibility of finding a wage growth norm that would be compatible with economic conditions across the Euro zone. This is illustrated by the divergence in wage norms that has characterized national-level bargains in the member states since the onset of EMU. In 1999, for instance, German unions began the bargaining round with demands ranging from 5.5% to 6.5% and managed to reach settlements averaging 3.1% in real terms (EIRO, 1999b). By contrast, the Italian metal sector union sought and achieved a 1.5% real wage increase, and Spanish metal sector real wages rose by less than 1%. In 2000, despite a generalized economic slowdown, pay increases continued to vary significantly, averaging from 5.5% in Ireland to as low as 1.8% in Italy and 1.6% in France in nominal terms, and from 1.1% in the Netherlands to –0.7% in Italy and –0.5% in Spain in inflation-adjusted terms (EIRO Online, 2001).

This variation in wage developments manifests how difficult it would be for social actors across the Euro zone to agree to wage targets at the EU level. Indeed, although the implementation of EMU creates a problem of fragmentation in wage bargaining that makes it difficult for the ECB to choose a target and for unions to assure their members that there is a payoff for wage restraint, it also sets national unions into a competitive game vis-à-vis each other. This effect is likely to be particularly pronounced in lower wage countries whose economies stand to pay the price (in terms of potential employment losses) in any effort to establish consistent wage growth targets for the Euro zone. Thus, although German unions have pushed for wage coordination across the EU to avoid regime competition, the principal impact that EMU has had so far outside Doorn Declaration countries (and even within some of them) has been that of promoting national social pacts. These national social pacts in many cases make direct reference to European parameters and, in this sense, may be thought to represent a form of "Europeanization" of bargaining (EIRO, 1999a). But they do so with an essentially defensive, rather than integrative, intent.[12] The common thread to these agreements is that the national level of bargaining has come to be seen as an indispensable tool in maintaining national competitiveness in the absence of national monetary and exchange rate options.

How then is the problem of coordination between wage bargaining and monetary policy in the Euro zone likely to be resolved? One alternative advanced by the EU Commission is to coordinate bargaining at a regional level, bringing together regions in different member states that share fundamental characteristics (industrially advanced areas vs. economically lagging areas). Such a scheme, however, has little support from national unions, who continue to view national sectoral bargaining as a mechanism to achieve cross-regional wage equality within their territories. Nor has it received support from employers.[13] The most likely effect of EMU on bargaining practices in the medium term is thus likely to be a reaffirmation of the trend toward national-level bargaining initiated during the run-up to monetary union in many member states. Increased pressure in favor of national bargains became apparent in the first months of EMU, as some countries (i.e., Ireland and Spain) began to experience a surge in inflation when the ECB cut its rates in response to price signals from other economies. Recent efforts to reach a national incomes policy agreement in Germany (within the context of the "alliance for jobs," which the employers and government would have

11. Representatives of the Italian and Spanish confederations, for instance, saw the shift to European bargaining as a logical extension of the move to EMU. But they adamantly rule out the possibility that such a development could take place in the short or medium term (interviews conducted in Madrid in May 1999 and in Rome in June 1999).

12. Examples range from the Belgian agreements, which preempt wage increases exceeding those in Germany, The Netherlands, and France, to the adoption of a "European" inflation rule in Italy.

13. Italian employers in 1999 rejected a call by a government commission for more regional-level bargaining within Italy, preferring the existing two-level (national sectoral/company-level) structure. The Spanish experience has been that regional bargains, in both poorer and richer regions, yield higher settlements than national sectoral agreements (CEOE, 1999).

liked to extend to wages) also suggest that, as traditional modes of macroeconomic governance are disrupted, the search for bargaining arrangements that emphasize the national dimension may also become increasingly relevant in some of the more "organized" economies of the EU, where coordination was previously achieved by other means (such as pattern bargaining in the German case).

Yet how would such a nationally centered pattern of bargaining affect monetary policy objectives in the Euro zone? From the standpoint of coordination, it might render positive results if it allows the ECB to focus on a lead country (or core of countries) and if national-level bargains in the rest of the Euro zone aim primarily at maintaining wage competitiveness in relation to that core. This appears to be the emerging pattern in the first 2 years of EMU, with the signatories of the Doorn Declaration seeking to match German wage increases and other countries seeking to compensate for excess inflation in their territories through more competitive wage bargains (the most recent example of this is the 2002 wage accord in Spain).

The cohesiveness of any such two-level model of coordination, however, will depend on a number of exogenous factors. One is the configuration of economic conditions between the Euro zone's core and its periphery. In the initial period after the onset of EMU, most periphery countries experienced an acceleration of inflation while conditions in the Euro zone's core called for a more lax monetary stance. This lent itself to the kind of "peripheral coordination on the core" just described. If the scenario were to reverse, however, bargaining in the periphery would not be able to compensate for an overly tight policy stance by the ECB. A second factor involves the behavior of unions as it relates to (a) the conflict between exposed and sheltered sectors and (b) the temptation to free ride on the fact that the ECB is not likely to raise interest rates in response to settlements covering just a portion of workers in just one country. The question here is whether the incentive faced by unions not to surpass (or even to undercut) settlements in other countries to maintain employment will eliminate this temptation. The record on this point so far is mixed. Thus, although during the first year of EMU (1999) overall wage growth in the Euro zone was noted for its moderation, averaging 2.7% across the Euro zone, in 2000 (a year of economic slowdown) the average rose to 3.1%. Last, a third condition for an effective two-tiered bargaining coordination game in the Euro zone is the consolidation of bargaining within each member state (as without cohesive national bargaining, coordination on a lead country would not be possible). The principal threat to the ECB's operation thus might come not so much from an overregulation of European labor markets as from any persisting underorganization of bargaining actors and fragmentation of bargaining within the member states.

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