

European Strains

An interdisciplinary research proposal on crises, institutions, and changing social models in Europe

Europe is in flux. Its institutions are subject to strains. The economy is marked by crisis, mass unemployment, indebtedness, and no growth. The welfare state provides insufficient protection. Citizens show social unrest and anger. Yet the present problems should be viewed in the light of past achievements. Most observers praise how the European economic and political integration has produced large gains for its citizens. The concern is now whether European integration is built on fragile compromises that only work in times of prosperity, or whether European institutions show more stability once they pass the phase of trial and error.

Integration has no doubt brought the European countries closer together but efforts meant to coordinate some policies have failed to coordinate others. Monetary policy and exchange rate policy, for instance, have been lifted up to the EU level, while fiscal policy and wages are still determined at the national level. Excessive fiscal policies and wage growth have therefore not been met by higher interest rates or a depreciating exchange rate. The Greek government could therefore accumulate huge debt while the private sector became less competitive. This is in sharp contrast to Germany where wages and spending have been held in check. The varying experiences and the resulting strains raise important questions about national institutions of collective bargaining and wage coordination.

With further integration, the EMU countries face harsher competition, while central macroeconomic tools are outside national control. There are strains related to fiscal harmonization, the four freedoms, welfare policies, and rising inequality. Wage inequality can perhaps be offset by workers moving to regions where wages are higher, while capital moves where wages are lower. But the movement of capital and workers may equally well reinforce each other, splitting Europe in booming and declining regions.

To explore these issues we need analytical approaches that combine the perspectives of cooperation, competition, and conflict with a passion for descriptive details and empirical studies. To do all this we need to involve several disciplines and their perspectives. To put it bluntly, it is equally wrong to study Europe with pure economics, abstracting from all institutional arrangements, as it is to concentrate all research effort around central EU institutions only. What is needed is an integrated social, economic and institutional approach, combining theoretical perspectives and empirical studies of several disciplines that together are able to eliminate the short-comings of each.

Our research outline proposes just that. It builds on the long run research commitment of ESOP (at the Department of Economics, University of Oslo) to study society models, labor markets and welfare states. We plan to combine this commitment with an active collaboration with some of the best scholars from the Institute of Social Research (ISF), FAFO, and the Frisch Center and from the departments of Political Science and Social Anthropology at the University in Oslo. The team members have a longstanding commitment to the study of European issues. Two core team members took part in "The EEA Review Committee" producing the recent whitepaper *Europautredningen* (NOU 2012:2). Together we all enter into a binding collaboration with top researchers from Dartmouth College, Graduate Institute of International and Development Studies Geneva, Hans Böckler Stiftung Düsseldorf, Harvard University, Institute für Arbeitsmarkt und Berufsforschung Nuremberg, Institute of Economic Analysis in Barcelona, London School of Economics, University of Amsterdam, University of California at Berkeley, University of California at Irvine, University of Milan, University of Oxford, University of Warwick, Stockholm University, and US Census.

The international collaboration allows us to work directly with linked micro-data on firms, establishments and individuals, comparing the pre- and post-crisis experiences in countries as diverse

as Germany, Portugal, Spain, Norway and the US, in addition to survey and more aggregate data that are generally available to researchers.

In sum, the proposal comprises expertise from Economics, Political Science, Social Anthropology, and Sociology. The aims are I) to understand the current crisis and its institutional responses, emphasizing the interaction between politics, economic development, and social change; II) to understand European migration, mobility and economic growth in the light of national identities, and social and economic strains; and III) to understand the economic and political feasibility of the European Social model, emphasizing how temporary shocks may create permanent institutional changes once we incorporate economic, social, and political reactions.

I. The Crisis and Institutional Responses

Institutional change that prepare for new policies, can be more important than the crisis policy itself. Economic, social and political adjustments in the short run can have lasting consequences.

Crisis as the mother of social reform

(Knutsen and Moene)

Under what conditions can economic and social crisis be conducive to productivity enhancing reforms? Many believe that crisis is the mother of progressive reforms and new social pacts. It is certainly not a general phenomenon that crisis lead to better political equilibria in the world. In much of Latin America, for example, the Great Depression led nascent democratic governments to be overthrown and to the emergence of an inward looking authoritarian development strategy that probably significantly retarded economic growth during the second half of the 20th century.

Our basic assertion is that the institutional response to the crisis reflects more the local national conditions prior to the crisis than the crisis itself. For instance, prior to the Great Depression the class struggle in the countryside were contested in Germany, Italy and Spain, while it was settled in the Scandinavian countries of Denmark, Norway and Sweden. Landownership in Scandinavia was rather egalitarian and the rural class struggle not very intense. In Spain, in contrast, the campaign for land reform in the South antagonized peasants even in the North (Luebbert 1991, Roemer 2001).

Economic crisis may increase the probability of governments exiting office through election, institutional reform and even democratic breakdown (Powell and Whitten 1993, Przeworski and Limongi 1997, Kennedy 2010). Which institutional configurations are involved? New extensive data projects open up for more detailed empirical studies of the determinants and consequences of particular institutional structures. One data project, the Varieties of Democracy project, codes 396 political and institutional indicators and is global in scope.

Our project member Carl Henrik Knutsen functions as Regional Manager for Western Europe for this ongoing effort, and will have early access to the Western European data. Importantly, these data extend back to 1900, and thereby allow for incorporating data, for example, from the interwar period - a time period in which the Great Depression is widely assumed to have affected European politics and even contributed to democratic breakdowns.

Thus, one part of the projects aims at studying how economic crises, low growth and high unemployment, affect particular political-institutional changes such as institutional checks on executive power, institutional guarantees of civil liberties and power-sharing arrangements in Europe. We are also studying alterations of the election system. The differences between plural-majoritarian voting and proportional representation are instructive. While plurality-majoritarian systems often lead to single-party majority governments, proportional representation may lead to frequent coalition governments. Again, institutional change in one area may induce institutional changes in others. Hence, temporary crisis may have persistent effects. We are interested in the broader political and institutional changes over the long-term, and will emphasize the implications for current reforms in European countries.

The effects of the crisis: Wage and employment responses

(Barth, Bratsberg, Cardoso, Card, Davis, Dustman, Freeman, Haider, Moene and Raaum)

The flexibility and adaptability of the European labor market depend on how wages react to economic shocks and how firms adjust their workforce. Within the enlarged euro zone, either wage adjustments or labor mobility is needed to avoid persistent high unemployment when countries face differential change in housing markets, financial markets, public finances and product markets. Many observers claim that in addition to poor macro management by governments, the failure of wages to adjust to differential development in labor productivity is an important factor underlying the present imbalance across European labor markets.

The rise in overall unemployment due to adverse shocks also depends on the hiring and firing decisions of firms ("labor hoarding"). Institutional contexts and policies generate variation in firms' incentives to retain workers during slowdowns with reduced labor demand. The analysis of how wages and employment respond to conditions in the labor market is one of the longstanding questions in economics and is crucial for our understanding of both macro and micro performance (see Blanchard and Katz 1998, Card 1995).

The crisis related labor demand collapses of Europe and North America provide a unique opportunity to explore how wages and employment respond to changes in economic conditions. Linked employer-employee data from Portugal, Spain, Germany, Norway and the US are now available for comparable analysis. These countries have been hit differently by the current crisis, have adopted different strategies to cope with the crisis, and operate under different institutional settings regarding labor markets and wage formation.

We plan to estimate how individual wages respond to the crisis. What types of establishments have cut back on wages and for whom? Does the cutback depend on skill types, newcomers vs. insiders, contracting firms vs. growing firms?. How do wages react under different institutional arrangements and macro policies? A study of how wage setting institutions (minimum wages and bargaining structures) may have changed will be an integrated part of the analysis.

Our aim is to derive implications for both wage inequality and for the general performance of labor markets in Europe, both in terms of allocation and adaptability to shocks. We draw on methods developed in the wage curve literature, where team members have made significant contributions (see, Card 1995, Dustmann et al 2010, Barth, Bratsberg, Naylor and Raaum 2002, Bratsberg, Barth and Raaum, 2006), on rent sharing (see Card et al. 2010, Barth, Bryson, Davis and Freeman 2011), wage inequality and institutions (Freeman 2007), the literature on nominal wage rigidity (Holden and Wulfsberg 2009) and on ongoing work on the US experiences after the great recession. The team consists of experts on the data for each country, with access to linked employer-employee data from before and after the 2008 breakdown.

We also want to explore the relationship between economic openness and wage coordination. Contrary to what many claim, more trade dependence seems to lead to wage compression and it seems to be wage setting coordination that drives it. If true, why does openness lead to higher levels of coordination? We have started with some tentative theoretical and empirical explorations (Barth and Moene 2012). Our basic assertion is that openness induces wage coordination because competitive pressures from abroad make collaboration between workers in exporting industries and the employers more likely. This implicit coalition is formed to 'control' wage setting in sheltered industries. Recent changes in Europe can indicate that we now might see more small open economies without wage controlling institutions.

The effects of the crisis: EU legislative politics

(Hix and Høyland)

How does the economic crisis change legislative politics in the EU? In particular we are interested in the effect on coalition-formation and voting-cohesion in the European Parliament. The assertion is that the crisis has challenged the ability of transnational political groups to act cohesively. The crisis has thus reduced the degree of ideological based policy-making and coalition-formation and shifted the balance in the direction of national interests and intergovernmental bargaining. As such it presents a challenge to the functioning of the European Union as a democratic system (Hix and Høyland 2013 and Hagemann and Høyland 2010)

We plan to explore how the effects of the institutional changes arising from the Lisbon Treaty, are separated from those of the economic crisis, in particular the reform of the budgetary procedure and the extension, the ordinary legislative procedure, of co-decision to all policy-areas. We also plan to explore the consequences for the implementation of EU directives in Norway, and to investigate whether the crisis has had an effect on the number of EU legislation produced, and their nature. To what extent has the national parliamentary involvement in transposition been altered?

To address these issues we are planning to develop a database on EU legislative politics, consisting of information on a) legislative acts and their passage through the legislative system, b) national transposition, and c) detailed information on political parties. This database will enable us to compare the political effects of the crisis on different parts of Europe. It will enable us to address questions related to political shifts and likely policy trends in the coming years. Will EU become more of a transnational arena, or will it primarily function as a mediator between conflicting national interests?

The effects of the crisis: European social values and social cohesion

(Barth, Finneraas, Hylland Eriksen, and Moene)

Another way of approaching the social effects of the crisis is to use survey data on peoples' attitudes and perceptions. Such changes in attitudes and perceptions may be the precursor of political change. In the World Value survey people are asked about their trust in relation to various persons and institutions; their attitudes regarding income differences; and their support for redistributive policies. The European Social Survey asks similar questions. Both surveys are collected before and after the onset of the crisis.

We plan to utilize panel data techniques to estimate the effects of changes in relative earnings, both within and across countries, on attitudes and perceptions towards institutions, income differences and redistribution. The International Social Survey Program (ISSP) has a Social inequality module in 1990, 1999 and 2009 on the willingness to pay taxes and redistributive aspects of taxation. The large and internationally comparative data, also contain rich information on individuals and their social positions.

There are indications that the crisis has changed social preferences of people. The change seems to go in the direction of more individualism, less care for others, to the extent that people trade equality for efficiency. One such indications comes from experiments in laboratory dictator games (Fishman, Jakiela and Kariv 2012). Comparing the behavior of similar subjects before and after the onset of the crisis, the researchers conclude that the crisis led to a dramatic reduction in altruism. We plan to explore this assertion further. If true, it highlights that social care disappears when it is most needed, complementing our explanations for why the support for welfare spending and political support for left-wing parties declines as inequality goes up, and as average incomes decline (Barth, Finneraas and Moene 2012). This is in line with theories of social identification emphasizing how the rich identifies with other rich, and how the poor are not identifying with other poor, but rather with the nation.

We also plan to explore systematic differences between countries and subnational groups and regions to account for the different reactions to the crisis. We will in particular look for new economic strategies (in the formal as well as the informal sectors) and the emergence of new forms of identity politics (such as various forms of nationalism). The comparative dimension will be essential throughout.

This subproject has an immediate link to the ERC funded 'Overheating' project, directed by Thomas Hylland Eriksen, concerning local reactions to global crises in five locations across the globe.

The contribution from social anthropology to our project consists of a two-year postdoctoral fellowship. The fellow will in cooperation with Hylland Eriksen draw on a broad range of published ethnographic case studies and other material to analyze the significance of culture and identity in the context of European crises and European (dis-) integration. The social anthropology group will also be central in other related research topics within our overall project.

The effects of the crisis: collective bargaining by riots

(Gates, Mehlum, Moene and Skaperdas)

The financial crisis and the euro crisis seem to undermine trust and social cohesion. Instead there are in many places social unrest, riots and anger. Workers across Europe have staged protests against austerity policies, and more generally against falling living standards. Recently more than 40 unions in 23 countries took part in 'a day of action and solidarity'. The protests range from general strikes to declining collaboration at the firm, industry, and national levels.

The social anger might be easy to understand. Yet we are interested in exploring several questions. One question concerns winners and losers: To what extent do the winners of the development that caused the crisis differ from the losers of its consequences? Another question relates to the possibility of a strategic element in sharing the debt burden. To what extent do organizations and governments apply a tactic of collective bargaining by riots? What are the effects of riots and protests on the terms of the individual countries? Such effects may be hard to identify empirically, increasing the importance of the theoretical framework. We are also interested in how conflicts over fiscal policies and sharing of the debt burden spill over to conflicts over other policies.

We plan to explore the causes and consequences of rising strike incidences in several European countries. What are the consequences for choice of production techniques, social efficiency and income distribution? When firms are faced with strike prone workers, innovations and firm design are likely to be inspired by distributional rather than technological considerations. There are at least two competing assertions (an discussion is provided in Moene 2011). One emphasizes the control of worker militancy. Thus strikes and strike threats induce labor saving innovations, and firms install more capital intensive production methods in order to replace at least some potentially revolting workers. The other emphasizes flexibility against work stoppage: Strikes and strike threats induce capital saving innovations, and firms install more labor intensive production methods. The idea is that faced with strike prone workers, the firm chooses a design that mitigate the economic consequences of militant workers. To do this they design the production process to increase its flexibility in the case of work stoppages. The aim is to reduce the effects of strikes on the profitability of the plant.

We plan to explore these ideas in the light of what we fear can be reemerging conflicting labor relations in Europe. Work stoppages can make the use of advanced capital equipment more expensive. Applying less efficient labor intensive methods enable the firm to cut costs during conflicts. Hence, more strikes may raise the de facto cost of capital, reducing the competitiveness of European firms.

This part involves two prominent conflict researchers: Greek economist Stergios Skaperdas from University of California, Irvine and political scientist from PRIO Scott Gates. They will contribute with expertise on violence, conflict dynamics and escalation, in particular in relation to riot-policing and riots as in English cities and in Greece, and also in relation to authoritarian political movements like Golden dawn.

The effects of the crisis: Macroeconomic policies in a union

(Holden, Mehlum and Moene)

The introduction of the common currency is the most important milestone in the European integration. When the European Commission lists the benefits of the euro it boils down to increased transparency in addition to the symbolic value of issuing one of the world's major currencies. These benefits may be substantial but the challenges and problems might prove to be even larger. We want to explore how this cross country fusion of monetary policy works with fiscal policy still at the country level.

After the financial crisis there has been much more active fiscal policies across Europe. Several countries counteracted the crisis downturn with expansionary tax cuts and government investment programs. In recent years, many countries have had serious problems with the resulting high deficits and growing government debts. The response has been to implement quite contractive policies. This shift in macro policies from expansion to contraction highlights important questions. How does national fiscal policy function in integrated economies with centralized monetary policy? To what extent does the sovereign debt of a country become a liability for other countries? This raises issues related to the workings of fiscal policy in itself and to the political economy of macroeconomic policies in a union with national fiscal policies and shared monetary policies.

We plan to carry out several research projects on the effects of fiscal policies. One project will follow up Holden and Sparrman (2012) and Brückner and Pappa (2012), and discuss the consequences for unemployment of higher government spending. The impact on unemployment may be quite different from the impact on production because of productivity differences between public and private sectors. In addition, fiscal policy might affect labor supply. In times of crisis we therefore need a separate analysis of unemployment.

We also plan to develop indicators of fiscal policies (see Girouard and André 2005). In order to identify the fiscal policy one has to discriminate between changes that are the results of policy and changes that simply are direct consequences of the business cycle (Braconier and Holden, 1999). The purpose of the new indicator is to get a more precise measure of the policy. We also want to explore the different effects of an equal amount of tax hikes versus expenditure cuts. Some studies show that a cut in expenses is the most effective way to reduce the deficit (Alesina og Ardagna 2010, Romer and Romer 2010). These studies suffer from problems with methodology and the coarseness of the indicators. We plan to explore these important issues with improved data and better methods.

Monetary authorities at the country level constrain what actors can do. A national monetary authority, that is set to control prices or the real exchange rate, will typically provide a direct predictable feedback from macro imbalances to the budgets of households and the government. We want to investigate the consequences for the political economy of macro policies and wage negotiations when the potentially disciplining effect of monetary policy is weakened by a fusion of monetary authority.

How is, wage growth and budgetary discipline affected when the monetary policy is centralized? Building on previous work (Moene and Wallerstein 2003) using cooperative game theory, we want to explore the strategic interactions between different economic institutions. Using the fiscal indicators, we plan to carry out cross country comparisons of how fiscal policy is conducted in countries inside and outside EMU. We plan to compare how wage setting is affected across sectors across countries.

The effects of the crisis: How soft is the European cushion? Earnings instability and income replacement in European welfare states

(Havnes and Solberg-Johansen)

The income instability faced by individuals and households is both a key determinant of policy and a major policy concern. How much does the earnings instability translate into instability in disposable income in the different countries? How important are household adjustments to cushion against the

earnings instability as compared to taxes and transfers, and how does this varies across European countries?

On the one hand flexibility in earnings is argued to be an integral part of a flexible labor market and of the creative destruction that reinvigorates an ailing economy. On the other hand, large swings in income may have high costs to individuals. Indeed, the larger is the instability they face, the stronger should be the tendency of individuals to take action in order to avoid this instability. This is of particular concern in an integrated European labor market, where an important way to avoid such instability may be to migrate to a different country.

Given the salience of the issue in policy, it is surprising that we know so little about how income and earnings instability differs across Europe. Most of what we know is based on cross-country comparisons of institutions and welfare systems. While one can point to many partial differences, the overall picture is hard to grasp: Tax and transfer systems are complicated and hard to compare; private responses to the system may offset (or sometimes magnify) the impact; and public services are hard to measure, let alone compare.

We take a different route. Instead of comparing features of the systems (inputs), we want to estimate the instability facing individuals in different countries directly, by considering variation in earnings and income over time (outputs). Following Blundell et al. (2008), we want to estimate the permanent and transitory earnings instability faced by individuals, using repeated observations of the same individual in a panel data set. The variance of earnings in the cross-section is informative about the overall level of instability. The covariance of earnings between periods in the panel is informative about the instability due to permanent shocks. At the same time, we may estimate how changes in earnings translate into the household's disposable income, by considering the covariance of earnings and disposable income in different periods.

We use the European Community Household Panel and the European Study of Income and Living Conditions, which provide panel data for many European countries over 1994-2010. This allows us to estimate both the level of permanent and transitory components in earnings instability, and the transmission to disposable income. Because the data also provide information about spousal earnings, we may further decompose the transmission to investigate the importance of self-insurance within the household compared to insurance via the tax and transfer system.

II Migration, Mobility, and Growth

Before the euro the development in Europe was marked by convergence across countries. Now, the development seems to be marked by more divergence (Midelfart (Ulltveit-Moe) et al 2002a,b).

How will Europe restore growth and employment?

(Golombek, Moxnes, Røed and Ulltveit-Moe)

Emerging markets challenge Europe's competitiveness in manufacturing. Almost none of the world's recent entrepreneurial success stories have taken place in Europe. If we go back 100 years we find Europe in the lead of establishing large firms, but now Europe is clearly behind the US. Between 1950 and 2007 Europe gave birth to 12 new big companies, USA to 52 (Philippon and Véron 2008). At the same time the investment flows has been reversed, now going from Asia and Latin-America to Europe.

In the current crises, European governments have started policy reforms that may boost entrepreneurship. For such reforms to be well designed we need to know more about the determinants of entrepreneurial activities. The bulk of the literature is based on relatively aggregated data. Since entrepreneurship is about individuals, micro data is essential. We have access to a comprehensive Norwegian matched worker-firm data set allowing for an extended concept of entrepreneurship including self-employment and limited liability companies.

The Frisch Centre has already used the data to characterize successful entrepreneurs (Berglann et al. 2011). We plan to use the data to explore issues related to the role of regional effects (Parker 2009).

Some of our questions are: What is the regional distribution of entrepreneurs? Are there tendencies to agglomerations? Does geographical proximity to other entrepreneurs affect entrepreneurial entry and performance? We are also interested in entrepreneurial internationalization

In the current crises it is of particular interest to study how entrepreneurship can serve as a way out of unemployment. Job loss could be an important triggering event behind entrepreneurship in Norway (Skogstrøm and Røed 2010). We also want to investigate how changes in compensation structures (wage compression may affect entry into entrepreneurship. Our planned research may have implications for the assessment of public employment services and social insurance programs across Europe. We will also investigate the effectiveness of promoting job creation rather than job search.

Labor migration, structural change and firm response

(Bratsberg, Dustman, Dølvik, Moxnes, Røed, Raaum Schøne and Ulltveit- Moe)

Despite free labor mobility, the 1980s and 90s saw surprisingly little labor migration between European countries. This changed after the Eastern enlargement of the EU in 2004 and 2007. The enlargement led to substantial labor migration flows from the new members towards Western Europe. As member of the EEA, Norway too was affected by these labor flows. Together with Ireland, the UK, and Sweden, Norway immediately opened up its labor markets to the new labor migrants, while other EU countries enacted transitional periods with restrictions on free movement of workers. These national measures were maintained until 2006 in Ireland, 2008 in the UK, and 2011 in Sweden. In the aftermath of the crisis with rising regional imbalances, migration flows between European countries are expected to increase, but magnitude and skill composition are crucial for the effects of free mobility on both receiving and sending countries.

Labor migrant flows. Using data from the survey data *European Union Statistics on Income and Living Conditions* (EU SILC), we plan to analyze gross cross national flows across Europe, and to break the number down by skills. Data on migration flows by skill level are scant. In this project we also add information in EU SILC to make inferences on the flow of skills across countries in Europe as well, since it contains information on country of birth. We shall compare flows with incentives to migrate and how gains differ across skill groups by comparing wage distributions across European countries, focusing on wage differences between countries for individuals of similar skills. EU SILC is well designed for this purpose. It has a relatively large sample size, detailed information of skills as well as data on unemployment status and regional residence. In this way we are able to analyze how migration flows respond to changes in economic returns across and within countries, from the period before and after the onset of the financial crisis.

A second study focus on detailed worker flows to Norway. Unlike multi-country data, Norwegian register data contain detailed information on migrant flows by type, including new residents, temporary foreign workers and posted workers. We want to analyze crucial factors that affect these flows to Norway. More generally, we will focus on foreign “push factors” or institutional factors that affect work flows to Norway from different European countries. This analysis will be the foundation for impact studies in the next section.

Economic effects of labor market flows Worker flows across national borders trigger labor market adjustments in employment and wage structures as both receiving and sending countries experience labor supply shocks. Recent studies show that the post-EU-enlargement worker flows have affected wages and job opportunities in the receiving Western European as well as the sending East European countries (Dustmann et al, 2012). The impacts of such labor movements depend on the size and the skill composition of the migrant flows. Given that migrant inflows from the new member countries to Norway were sizeable both in absolute terms and relative to the existing labor force, one would expect significant impacts on the Norwegian labor market. This has also been documented in NOU 2012:2 , Dølvik et al. (2012).

Wage effects of labor migrant inflows to Norway are studied by Bratsberg and Raaum (2012) and Bratsberg et al. (2012), focusing on short-run effects. In the long run, economic implications of labor movements hinge crucially on the adjustments made by firms. According to trade theory, an increase in the supply of labor with sector-specific skills affects wages in the short run and resource allocation across sectors in the long run. Migration may trigger structural change at a relatively aggregated level, but it may also impact on the organization of vertical production networks: First, the incentives to (re)locate production abroad either through (foreign direct investment, or through international outsourcing) may change as relative wage costs respond to migrant inflows. Second, more abundant and cheaper labor resources raise the economic returns to investments in physical capital and technology.

The literature on the relationship between trade and firm performance is extensive and growing (see Bernard et al. 2007 for a survey). There are also discussions of how different types of trade shocks have affected firms (Ekholm, Moxnes and Ulltveit-Moe 2012). Behavioral responses of firms to labor migrant mobility, however, are difficult to study empirically, requiring detailed data on firm investments and a credible identification strategy. Apparently, lack of linked worker and firm data have so far prevented scholars to analyze migration shocks on firm performance. The extraordinary register data in Norway, in combination with the shocks following the EU enlargement, offer a rare opportunity to study decisions by firms. The insights from this study are therefore of general interest as it is likely to provide new evidence on the long run effects for receiving countries

We have access to Norwegian Employer-Employee data for workers by national origin, including temporary and posted workers. As these data today cover the years 1992-2011, we are able to study changes within and across sectors and firms following the enlargement of EU in 2004, focusing on a set of research questions:

We will use information on wages of natives, earlier immigrant cohorts, and the new labor migrants in combination with employment records to address the following questions: How does labor migration affect pay structures across firms and industries? How does labor migration affect structural change and allocation of labor resources across industries and sectors in the Norwegian economy?

We will use employer-employee data matched with a set of data sources on firm characteristics, like firm economic performance and exports, imports and foreign investments to investigate What are the effects of the supply shock in the Norwegian labor market incurred by Eastern European migrant inflows?. Can the differences in wage growth, employment, investment and internationalization strategies between firms be explained by differences in the exposure to labor migration?

Our empirical results will give important insights in the impact of migration on the Norwegian economy.

The European future: towards divergence or convergence

(Baldwin, Forslid, Javorcik, Ulltveit-Moe and Venables)

Around the times of establishing the single market and establishing the single currency, the consequences of these reforms were extensively discussed. Particular emphasis was put on the question of whether the reforms would foster convergence or divergence. With Europe in a middle of crisis it is of importance to revisit these questions again, and investigate how measures that would contribute to the completion of the monetary union (e.g. fiscal harmonization) and further realization of the four freedoms (i.e. free mobility of goods, services, people and capital) affect economic development and inequality across European countries and society groups.

Will we see enhanced or reduced inequalities? What policy initiatives will affect whether we move in one or the other direction? To understand better what initiatives that will foster divergence rather than convergence, we also need to examine the relationship between economic shocks and spatial dynamics. There have been studies at the state as well as county level of the US investigating the spatial dynamics

of shocks that typically tend to hit regions differently, see e.g. Blanchard and Katz (1992) and Fogli and Perri (2012). Analyses at the state level tell us that labor migration may contribute to convergence in income. However, evidence from the county level suggest that the impact of neighboring counties on own economic development may be ambiguous and depends on the magnitude of the recession. Using European regional economic data in combination with labor market surveys we want to investigate the economic geography of business cycle dynamics in Europe. Such analyses may provide important background for the formulation of macroeconomic policies.

III. The Future of the European Social Model

A central aim of European integration is to promote the so-called European Social Model. Although Europe has been known for its different families of welfare states, collective bargaining, and labor market regulation, most EU and EFTA countries have been characterized by quite encompassing systems of social protection and income security, management-labor relations governed through collective bargaining and social partnership, and extensive employment protection legislation (see G Esping-Andersen (1990) Hyman and Ferner eds.(1998)) When promotion of the European Social Model became one of the main EU objectives, the national social models faced new challenges and constraints emanating from the process of European integration itself and from broader global dynamics.

Multilevel governance of European labour markets: National and European responses (Dølvik, Eldring, Evju, Meardi, Keune and Schulten.)

In a number of projects we plan to study how institutions change at the level of nation-states and at the supranational European level.

In welfare policies, the EU has no legislative mandate, but seeks to promote convergence through soft methods of coordination. A multilevel European system of social and labor market governance has therefore evolved, in which the nation states remain the locus of regulation and policies, complemented by European minimum standards and rules determining the laws and conditions that are to apply for different categories of migrants and cross-border workers. Non-working migrants and workers being employed by an employer established in the host state, posted workers sent by a foreign services provider or a temporary work agency, and self-employed, are subject to different rules regarding social rights, wage setting, social security, and hence labor costs. Given the discrepancies in home and host country standards, this provides ample room for strategic adjustment by employers and workers as well as citizens searching for better welfare provision ('regime shopping').

Comparing changes in the Nordic countries, UK, Germany, the Netherlands, Italy and Poland, the study will concentrate on the following main issues:

1. Mapping changes in EU regulations of labor markets and cross-border work – focusing on their causes and likely consequences for different national systems;
2. Comparative analyses of key changes in national labor market regulation and institutions with emphasis on minimum wage setting – statutory or by extension of collective agreements – and the strategies/approaches of the trade unions and employer federations in this regard. This issue will be of high relevance for, and benefit from, the subproject on employer adjustments of wages and employment in different countries during the crisis.
3. Comparative case study of the implications of the currently implemented changes in the rights for temporary agency workers (flowing from the TWA-Directive EC08/104) and its interaction with the rights of posted worker (flowing from the Posting Directive EC96/71). Given the TWAs increasing, contested role as link between new channels of labor migration and new modes of more flexible hiring, how will the changes in regulation impact on patterns of recruitment, the conditions of migrant labor, and the role of trade unions and employers in determining conditions in this realm? This issue will provide useful input for the subproject in which the effects of such regulative changes for hiring and

wages of different (migrant) worker categories in Norway will be studied empirically by means of registry data.

A Common European Asylum System Amidst national divergence, international rights and migrant strategies

(Brekke and Brochmann)

The process of harmonizing migration policies and regulations within the European Union has come a long way since it started in Tampere in 1999. In 2012, the Union expects to finalize the second generation of a Common European Asylum System. One persistent challenge has been securing burden sharing among member states. There are substantial differences between the countries, creating incentives for secondary movements.

The field of migration provides an excellent opportunity for studying the discrepancy and tension between the supranational ambitions at the EU-level and persistent national differences. The ongoing economic crisis accentuates the national discrepancies in living conditions and level of social support for migrants in Europe.

We use the contrast between the Southern rim (Italy and Greece) and the prosperous North (Sweden and Norway) as the empirical basis for the study. Secondary movements within the EEA-area are indicators of regime competition and the concomitant migrant strategies. Our aim is to explore strains between the supranational and the national policy levels. Adding the migrants themselves we get three levels of analysis: *institution, policy and agency*.

We build on the research project “Migration to Norway” and ongoing studies of asylum journeys conducted (Brekke and Aarset 2009, Brekke and Brochmann 2012) to investigate the role of information, networks, and migrants’ perceptions of destination countries.

The three level approach inspires a set of research questions:

1. International and European Human Rights provide a framework for the development and practicing of common European standards. How do court decisions based on these norms influence the strategies of governments and migrants?
2. The situation with regard to reception conditions and later integration support diverges between the member states. In what ways do integration- and welfare policies impact on migrants’ strategies within the Dublin context, and opposite, how do prospects of reforms in the Dublin regulation influence the states’ policymaking in the same fields?
3. Asylum seekers, refugees and family migrants have knowledge about the Dublin regulation and its return policy to the first country of asylum (Brekke and Brochmann 2012). How does this knowledge influence their motivations, strategies and actions?

The paradox of welfare and the optimal unit of social policy

(Barth, Hylland Eriksen, Mehlum and Moene)

In all European countries there are strains in the relationship between the private and the public sector. We plan to explore what we denote the welfare paradox and to assess the magnitudes of the effects.

The welfare paradox can be presented by four observations. a) In contrast to welfare state *services* the production of private sector *commodities* are easy to mechanize. This effect, called the Baumol effect, favors the private sector. b) While the private sector produces tempting goods providing immediate pleasure, the welfare state produces services delivered without immediate consumer sovereignty. The temptation effect stages individual preferences in favor the private sector. c) As people get richer they demand relatively more services. This effect, related to the so-called Wagner’s law, favors the welfare state. d) Since both sectors must pay similar wages, the welfare state become relatively more expensive

the richer society becomes, making temptation goods cheaper and welfare services relatively more expensive.

As long as Wagner's law is not strong enough, the observations a), b) and d) lead to the following welfare paradox: *The willingness to pay for the welfare state declines with societies' capacity to pay for it.* The problem is caused by what we call the 'tyranny of mechanization', emphasizing how society becomes richer in a manner that makes labor intensive welfare provisions appear more and more expensive. Accordingly, each tax payer must give up more and more of the temptation goods in order to pay the taxes to fund the welfare state. We believe that the welfare paradox also speaks to the present crisis in Europe, and that it is more evident in some countries than in others.

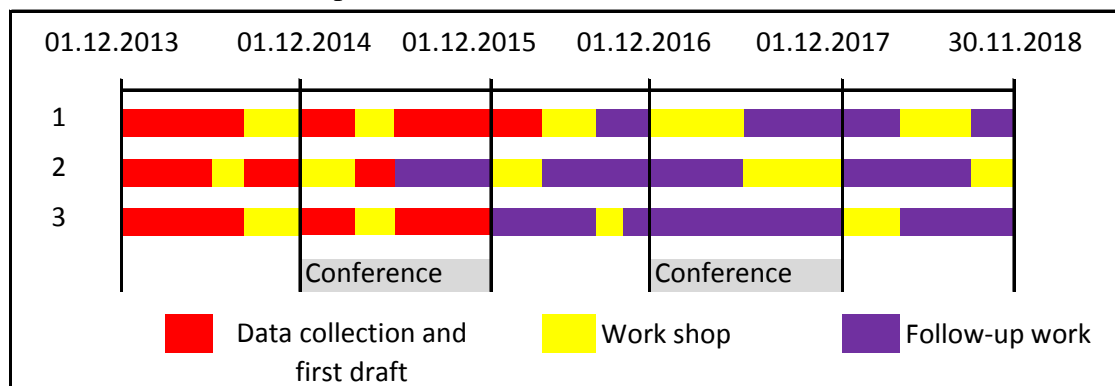
The paradox of welfare also has implications for possible reforms and for the future of the European social model. For instance, what should be considered an optimal unit for the redistribution and social insurance when the policy requires majority support? Is it the family, the commune, the national state, the EU, or the world?

The basic trade-off seems to go between the size of the insurance pool which increases with the unit, and the intensity and commitment of social care for the participants which declines with the size of the unit. Clearly, the family is not an optimal unit for redistribution. The social care for other family members is high, but the insurance pool is too narrow. Extending the insurance pool by moving to larger units would at the same time lead to a lowering of the social care for other members within the unit.

Thus it is clear that the unit that for instances maximizes redistribution in favor of disadvantaged groups is not found in either end of the spectrum --- as long as the policies should obtain majority support from the electorate. It is most likely found at the intermediate levels. Whether Europe is the optimal unit, remains to be answered. Most likely this exercise, that we plan to carry out in detail, can provide information on what matters for the determination of the optimal unit, rather than providing a definite characterization of what the optimal unit is. Yet, speculative discussion like these might bring fresh insights to the ongoing debate about the future of the European Social Model.

Project plan and milestones:

The following chart shows the milestones for the research areas 1 to 3. It also shows the main conferences and workshops.



International and national cooperation and network building

ESOP, The Frisch Centre, ISF and Fafo are very proud of having such an excellent group of researchers who all are well established and internationally oriented ---and many of whom are leading female scholars, including Grete Brochman, Karen Helene Ulltveit-Moe, and Marianne Røed. In addition we have as active, contributing members of our team well renowned international scholars, Richard Baldwin, Ana Rute Cardoso; David Card; Christian Dustmann, Richard Freeman, Stergios Skaperdas, Anthony Venables, They are not only world class academics, but are also scholars with a deep empirical knowledge about labor issues and social issues. More generally, all participants in our project group have extensive international networks both in social sciences in general and in European issues in particular.

Budget

The total budget of the project is NOK 34,075 million. We propose to use the funding from RCN of NOK 24 million, and our own funding from ESOP and The Department of Economics, UiO of NOK 10,075 million, over the 5-year project period as follows (all amounts in NOK):

Personnel resources	16 883 000	
Travel (own travel and guests)	1 000 000	
International Conferences, workshops and data sets	1 644 000	
Procurement of R&D services	14 548 000	
Frisch Centre (including one doctoral position NOK: 2 926 000)		(6 626 000)
ISF (4 000 000)		
Fafo (2 000 000)		
SAI (one post-doctoral position in two years) (1 926 000)		
Total project costs	34 075 000	

Own financing: ESOP and the Department will contribute with a total of 8,54 man years in the proposed project. In this contribution there is one of our PhD-students who is contributing with a total of 0,54 man year. In addition ESOP will contribute with a total of 240,000 NOK to other operating expenses over the five years the proposed project lasts.

Positions at ESOP, UiO covered by the Research Council

- 20 % visiting researcher position over three years
- 20 % Research assistant position over four years+

Procurement of R&D services covered by the Research Council:

-Parts of the research activity connected to this project are carried out by, The Ragnar Frisch Centre, The Institute for Social Research (ISF), the Institute for Labour and Social Research (Fafo), and the Department of Social Anthropology (SAI) at the University of Oslo. All proposed funding to these institutions are above shown as Procurement of R&D services. This budget post includes one Phd-position (stationed at The Ragnar Frisch Centre) and one postdoctoral position (Stationed at the Department of Social Anthropology). The rest is means to partial research positions, and visiting researchers at each partner institution, respectively.

Other operating expenses covered by the Research Council:

-travels (both guests and own), Workshops and conferences, and purchasing data sets to a total of 2, 404,000,- NOK over the five year proposed project period

Dissemination and communication of results

At least 40 high quality publications in international journals will be published. The project will host two main international conferences and several workshops each year. We will also arrange public lectures and seminars. All activity will be published at the webpage we are going to develop, and results from the project are going to be channeled through mainstream media.

Several of the participants have a record as a very visible contributors to the Norwegian and international media. Some of them have their own columns in Norwegian newspapers and several are op-ed contributors on a regular basis. All researchers connected to the project will continue to disseminate research results through the various channels of the mainstream media. In addition the results are to be presented on several conferences and workshops during, and after, the project period. The researchers are also generally forthcoming when interested groups ask for lectures or panel participation.

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