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How Shameless Copycatting Can Save Europe

by Klaus F. Zimmermann

Amidst all the pessimism that Europe is stuck in a rut, it is important to look at the pivotal ways in which European Union countries influence each other — and how those cross-border "learnings" move the entire European economy ahead. This is especially important at this juncture, because it points to very real-life paths out of the present economic conundrum.

Take the turnaround in Germany on the jobs front. These days, the country is widely considered a role model for successful labor market reforms. That is an astonishing development. A mere decade ago, Germany was often referred to as the "sick man of Europe." Not only did it suffer from high and persistent levels of unemployment, but its wage and benefit levels were so high that the country had catapulted itself out of the ranks of globally successful economies.

How did Germany get back on track? The official answer is a series of labor market reforms initiated in 2003 under the "Agenda 2010" framework. Unemployed individuals were given stronger incentives to take up jobs, and overall labor force participation rates increased.

However, the biggest credit should perhaps not go to the German government, but to neighboring Denmark. Why? In a telltale sign of how modern Europe really works, German labor market reforms adopted the "flexicurity" concept that is the hallmark of Danish labor market policies. This approach is sometimes described as "tough love." It offers the unemployed relatively high levels of financial support, as well as generous retraining opportunities. But it also obliges them to be proactive and very flexible in their job search. The goal is to ensure the actual time spent without a job is short, while the level of qualification (and compensation) is preferably kept up when a new job is found.

Wage restraint on the part of the trade unions also helped Germany regain its international competitiveness. However, contrary to what is widely believed, this was not the key factor in bringing about the decline in unit labor costs.

More important was the way employers and unions used the collective bargaining process to arrive at much more flexible labor arrangements. As a result, existing work processes, schedules, and procedures could be adjusted and reorganized not only, as before, at the industry or sector-wide level, but crucially also at the firm and the plant level.

This newfound localized flexibility is the real source of the German economy's new resilience. It has improved our economy's responsiveness to the vagaries and challenges of the global market.

And this is precisely where the dynamics of intra-European cross-border learning kick in yet again. The recent German experience is now being actively debated to the north, in Sweden.

Sweden is another strong export-oriented nation which, like Germany, has a healthy current account surplus and a stability-oriented fiscal and overall economic policy. In addition, Swedes have long prided themselves on pairing a thorough embrace of capitalism with an equally strong sense of social balance. Yet it seems as if Germany has managed to get ahead on this very issues, largely by applying a much more fine-tuned and open-minded level of cooperation between unions, employers, and the government.

Looking closely at the labor market innovations in Germany could help Sweden overcome some of its current core challenges. These include too high a level of employment protection, high overall labor costs, and a labor market that is regulated too strictly. Indeed, the current issues facing the Swedish labor market appear to be quite similar to the ones Germany faced in the 1990s.

The high level of youth unemployment in Sweden must also be a major concern. Such unemployment creates long lasting scars which can affect labor market outcomes much later in life. To avoid that, part of the answer is to take measures that prevent young individuals from finishing school without a degree and to smooth their transition into the labor market.

In that context, the German strategy, which focuses on vocational training, may be very suitable. Young people undergo a multi-year training program, blending firm-level training with time spent in technical schools funded by the government. This apprenticeship system is really one gigantic, all-hands-on-deck microeconomic management exercise that involves all the relevant stakeholders in society. That is a framework Swedes should quite naturally excel in.

But here again, the learning is not one-directional. Looking at its own present-day problems, Germany can learn some very vital lessons from Sweden. Sweden's labor force participation rates are high by international standards, in particular among women and older workers. The country also has a comparatively high fertility rate and a relatively high immigration rate. These are important achievements in preparing the country for population aging, demographic change and a shrinking labor force - the very issues Germany is struggling with.

In my view, Sweden's policy measures therefore ought to move right to the top of Germany's own reform agenda. If that happened, it would underscore the vitality of cross-border learning in Europe — and solve an important problems for Germany.

Ultimately, what is going on is best described in the words of a Scandinavian finance minister: "The reality is that all of us shamelessly copy and steal from each other whatever works well in other countries," adding, "That's what we should be doing all the time." Such copycatting is exactly what has to happen to stimulate the growth agenda throughout Europe.