

GENERAL REPORT ON FORUM 5

Emergence of convergence?

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If there is a central theme that runs through the many papers in Forum 5, it is a question. The papers of Forum 5 ask whether world employment practices are converging along various dimensions. Given that theme, it is somewhat ironic to be the rapporteur for this forum. I can remember presenting a paper at the Brussels meetings of the IIRA in 1989 with my co-author, Mahmood Zaidi. We argued in that paper that certain tendencies that had become evident during the 1980s in the U.S. were likely to be felt internationally. Among the tendencies we cited were de-unionization, union concession bargaining, greater use of contingent workers, and a general loosening of the employer-employee relationship.

Nowadays, the idea that such a convergence might be occurring is no longer considered peculiar. Certainly, the idea of studying the possibility of convergence is not odd, judging by the contents of Forum 5. But much of the audience reaction back in 1989 was skeptical. At best, the comments suggested, what we were describing was a uniquely American phenomenon with no general applicability. Yet today one has only to examine such publications as the recent World Labour Report of the ILO to see signs of de-unionization in most developed countries. And the other phenomena we predicted are also in evidence. Since having a narrow American view turned out to be a pretty good strategy in 1989, later in this report I will be even more narrow. I will take the perspective of a narrow Californian. But more on that below.

Various Forms of Convergence

Several forms of convergence were investigated in the papers of Forum 5. These can be grouped into five categories:

1) Convergence in terms of management style. This is actually an old question in the research literature, although one which should

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be kept up to date. Usually issue here is whether multinational companies (MNCs) export their home styles of management and labor relations to host countries. Whether or not they do so could be a Good Thing or a Bad Thing, depending on what you think about the style in question. Thus, the topic can be taken as a neutral, empirical examination. Do they or don't they?

2) Convergence in terms of economic security and social insurance. From the European perspective, this sort of convergence is often seen as a Bad Thing. The fear is that the existing system of job protections will erode under pressure of competition from countries with less generous approaches. The American perspective on this question has been more mixed, perhaps because the level of social protections in the U.S. is lower than in Europe. Indeed, some American researchers have instead used the onrush of international competition to highlight the cost of existing U.S. social regulations of all kinds. From this viewpoint, globalization has raised the cost of these social regulations which were already perceived as too high.

3) Convergence in terms of minimum labor standards. Here the issue is connecting some definition of basic labor standards to international trade agreements. The proposal tends to be seen as a Good Thing by many developed countries, although not all have aggressively sought to modify trade agreements accordingly. In contrast, in developing and emerging countries such proposals are usually seen as Bad Things and disguised protectionism.

4) Convergence in terms of typical labor standards. This type of convergence refers mainly to pay and work-related benefits. The concern in developed countries is that pay will be drawn down toward levels found in developing and emerging economies. But it may not be the pay of all workers that is the target of concern. Rather, it is sometimes argued that workers at the low end of the pay structure in developed countries are most susceptible to trade competition. Therefore, it is said, trade will widen (or has widened) wage inequality between the high and low paid. Of course, to the extent that the same competitive forces pulled up wages in developing and emerging economies, the impact might be seen as a Good Thing. Also covered by this topic is the possibility that unions could bargain internationally to achieve gains in pay and conditions.

5) Convergence in terms of mechanisms of employee participation. In this case, the focus has been primarily on works councils of the European variety. The issue is the degree to which such practices have been spread through legal regulation or by the employ-

ment policies of MNCs. In some cases, such works councils might be seen as an alternative to union representation. In others, they might be seen as forums through which unions could gain enhanced representation rights.

The Role of the Rapporteur

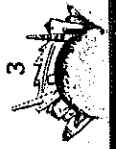
There are several roles that a rapporteur can play in these meetings. One obvious role, indeed a required one, is to summarize the papers within the forum. I will, of course, provide such a summary below, although I will try to be brief since abstracts of the papers are available. A second role is to offer opinions on the topics at hand. This role may not be required, but it is difficult to resist. Finally, there is a third role; that of pointing to areas that might have been explored within the forum but were neglected. I will also play this third role, introducing some new material and perhaps stimulating further research among members of this congress. By way of preview, I will combine the second and third roles in a section dealing with macroeconomic considerations. In my view, Forum 5 lacked an adequate macro perspective on the convergence issue. Especially lacking was discussion of the implications of the monetary union now forming in Europe.

Summary of Forum 5 Papers

It is important to note that at the point at which this report had to be written to comply with congress deadlines, not all papers from Forum 5 had been received by the rapporteur. And - in certain cases - only the abstract, not the full paper, was available. Some of these abstracts referred to work that had yet to be completed. Thus, the summaries that follow may not do full justice to the various papers cited as they will appear in their final forms. And papers not received by the deadline for this report are, of course, not reflected in the discussion.

• Convergence of Management Style

The issue of whether MNCs import their home-country style of labor relations is partly related to the degree to which such firms delegate responsibility to local management. Bélanger and his co-authors focus on this question. They examine unionized Canadian operations of Swedish/Swiss electrical equipment multinational,



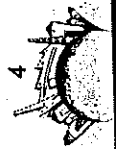
Asea Brown Boveri. Corporate headquarters has pushed an agenda of restructuring and total quality management. Bélanger et al find that there was some scope for influencing implementation of these policies at the local level. But the degree to which Canadian unions could bargain over the policies was limited. In the Canadian case, of course, there was no counterpart to the mandatory company-wide institutions found in the European Union (EU). And the labor side accords of the North American Free Trade Agreement (NAFTA) do not deal with such issues.

As luck would have it, Forum 5 contains a second paper - this one by Bray and Lansbury - dealing with the same MNC. These authors looked at Asea Brown Boveri plants in Finland, Australia, and Switzerland for their comparison. Their conclusions are much the same as those reached in the Bélanger et al study. Local practices matter but the thrust of corporate policy with regard to major human resource practices came from company headquarters in Zürich. The general direction, at least in this firm, suggests a movement toward centralization and convergence of employment policy.

Two papers - one by da Costa and the other by Tremblay - focused on the behavior of Japanese multinationals abroad. Da Costa studied Japanese metallurgy and electronic plants in Spain and France. She finds that they do not mechanically follow what is often viewed as the "Japanese model" of production. But internal communication is emphasized. However, the Japanese MNCs tend to have weak unions. Da Costa suggests that the impetus for the workforce to go along with such policies may stem from current high unemployment.

Tremblay's Japanese transplants were located in Canada (including Québec). She compared the transplants with non-Japanese firms which emphasized quality and with other firms operating without a special quality focus. Her study suggests that in many cases the Japanese firms were more like the "other" group than they were like the quality-focused firms. The Japanese firms did not seem to be exporters to Canada of the Japanese model of labor relations.

Huang's paper included both Japanese, German, U.S., and native firms operating in Taiwan. This study finds that the German and U.S. firms follow somewhat different practices than the Japanese and Taiwanese firms. That is, there seemed to be a western model and an eastern model. Nonetheless, all firms were subject to



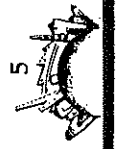
Taiwanese law with regard to such practices as layoffs, a fact that tended to homogenize their labor policies. Huang believes there are tendencies toward convergence in employment policy across all of the firms. The western firms were moving toward (eastern) internal promotion and the eastern firms were using such individualized (western) approaches as pay for worker performance.

Another Asia-based study, this one by Goodall and Warner, examined the operations of joint ventures in China. The comparison here was between state-owned firms and joint ventures. One might expect from popular media reports that the state-owned firms would all be unprofitable while that joint ventures would be efficient and profitable. But in fact there was a range of experience. Some state firms were operating in the red, as were some joint ventures. The joint ventures paid somewhat higher wages than state-owned firms and were somewhat less likely to have a collective agreement with an official union. However, all firms were being exposed to market forces and were moving away from elaborate schemes of benefits and job security. Pay systems and pay determination were increasingly dictated by labor-market needs. It may be that the joint ventures were not moving faster than the state enterprises because they all had inherited personnel managers brought up under the old system of state management.

Since it appears that who is in charge of personnel policy matters, the study by Chua and co-authors is especially relevant. In this study, a sample of U.S. expatriate managers was analyzed, indeed factor analyzed, to determine their ability to work successfully abroad. The authors note that expatriates are very expensive for MNCs but can be vital to firm performance.

The study appears to be largely a reduced-form exercise, i.e., a formal model of why certain practices might help or hurt the performance of the managers is not presented. It is interesting, however, to note that among the criteria for managerial performance were "tolerance for ambiguity" and "adaptability to host country's operations." Such criteria carry the implicit assumption that the role of the expatriate is not to dictate detailed policy. Some scope for local autonomy and practice must be allowed. On the other hand, use of expatriate managers suggests that MNCs are not comfortable leaving labor matters totally to local executives.

In summary, as a group these papers confirm results of previous studies. MNCs are a vehicle for convergence of employment poli-



cies. But they do not enforce a complete unification of practice across their foreign subsidiaries.

- **Convergence in Economic Security and Social Insurance**

One paper in Forum 5 most clearly represented the European fear that global market forces were undermining national industrial relations systems. Looise and van Riemsdijk argue that until recently, European countries were able to have their unique industrial relations systems, maintained by national legal constraints. Now MNCs all push for a "flexibility" which undermines local protections and social insurance. Corporate goals have become lean production, downsizing, restructuring to focus on core business advantages, broad definitions of work content, and pay for performance. Even if these goals are accepted, union cooperation in implementation would be desirable and beneficial to the workforce. But it is not clear to the authors that mechanisms are in place to obtain union cooperation or, indeed, to work with unions at all. Europe, they propose, must come up with its own alternative system or risk growth of poverty and income inequality. As promised earlier, I will return to this theme below from the vantage point of a Californian.

- **Convergence of Minimum Labor Standards**

There was substantial interest within Forum 5 in the establishment of minimum labor standards linked to international trade agreements. This topic is intertwined with the general issue of human rights as a condition for trade concessions. The interconnection is usually depicted as a purely moral issue. But it is interesting to note that some evidence has emerged suggesting a connection between human rights and tangible work benefits. A recent study, for example, finds a connection between wage levels and democracy in the political system. That is, controlling for economic conditions, democracies offer higher wages. In any event, were labor standards agreed upon and enforced through trade arrangements, they would - by definition - bring about a convergence of minimum conditions across countries.

In fact, although usually seen as an issue for developing and emerging economies, labor standards can be evaluated within developed countries. Thus, the paper by Block and Roberts applies a measurement tool to create an index of labor standard variation across Canadian provinces and the states of the United States.



Both countries, together with Mexico, are members of NAFTA. Not surprisingly, the authors find a higher level of standards in Canada.

Still, much of the controversy about labor standards has involved countries at different stages of economic development. Often the issue has been particularly centered on the emerging Asian economies which - before the recent financial crisis at least - were seen as shining lights illuminating the road to export-led prosperity. Coulthard points to the current debate about the possible linking of labor standards to the World Trade Organization (WTO).

Haworth and Hughes also explore the possible role of APEC in implementing or fostering labor standards. The International Confederation of Free Trade Unions (ICFTU) has been active in pushing APEC to consider the labor standards question. But key APEC members see APEC's role as promoting trade, investment, and development. With success in trade, investment, and development, it is argued, labor standards will rise naturally through market forces. Thus, APEC has rejected a WTO role in labor standards, arguing that such standards were the business of the ILO. But when the ILO began taking a more proactive stance on the matter, that approach was also rejected. Is it unkind to suggest that the Asian tigers prefer that the ILO tiger be toothless?

There is a kinder view, however. Perhaps the issue is that those countries that feel themselves most threatened by minimum labor standards proposals want a voice in establishing the standards. They do not necessarily want to adopt pre-existing ones. Tan Ern Ser suggests that a multi-country forum which collectively developed new standards could assuage fears that labor standards proposals were just covert protectionism by developed countries. It may be that the ILO needs to provide such a forum if APEC is unable to do so.

Now that the ILO has been thrust into the debate over labor standards and trade, it has had to move cautiously, as Trebilcock points out. At present, she characterizes the debate over labor standards as a "dialogue among the deaf." Apart from playing some role in the trade/standards link, the ILO has been interested in such issues as promoting social labeling.

Under this proposal, products would be certified to have been made, for example, without use of child labor. Another approach is to have MNCs agree voluntarily to codes of good labor conduct.



These approaches raise inevitable questions of who the certifying agent would be in the case of labeling and how the good conduct would be verified. Apart from promoting discussion of such interventions in trade practices, the ILO is studying the impact of international trade on national labor markets. Trebilcock also references studies by the Organization for Economic Cooperation and Development (OECD) concerning the labor standards issue. She characterizes these studies as taking a positive position on such standards. But I find OECD reports to be more ambiguous about the benefits of imposed standards than Trebilcock does.

Erickson and Mitchell note that the U.S. government has pushed for a labor standards/trade linkage. And within NAFTA, there are labor side accords. These accords were added after the treaty was signed under the pressure of the incoming Clinton administration. As Morgado-Valenzuela points out, NAFTA is not the only Western Hemisphere trade agreement with some reference to labor standards. The MERCOSUR agreement in South America also has some reference to labor standards.

Nonetheless, the NAFTA accord represents a different model of standards than the much-debated "core" approach. In essence, the three member countries of NAFTA have agreed to enforce their own labor laws. Mechanisms exist for complaints to be filed and investigated if such enforcement is not occurring. Although much of the complaining has been about Mexico, at least one complaint was directed at the U.S. under these procedures. Developed countries should thus be aware that the road to labor standards is a two-way street.

In the U.S., there have been fears that trade is bringing about wage inequality by putting downward pressure on the wages of the unskilled. International trade theory, notably the Heckscher-Ohlin model and later literature, suggests that such impacts could occur. Erickson and Mitchell find that U.S. trade pattern with China and the four Asian tigers (Hong Kong, Singapore, South Korea, and Taiwan) does follow Heckscher-Ohlin predictions. That is, the U.S. imports relatively labor-intensive products from these countries. But the wage impact is small (so far). The U.S. trade deficit may be a greater villain than the trade pattern per se in widening wage inequality.

The long-term wage impact of China, which is adding a huge labor supply to world competition, could be different and might have negative effects on wages in developed countries eventually.



But labor standards would have little impact on these tendencies and, Erickson and Mitchell argue, emerging economies which want access to developed markets should consider adopting some type of labor standards. Particularly with regard to access to the U.S. market, the alternative might be the kind of unilateral action to which the American Congress and legal system are prone. As Vause indicates, both American institutions (legislative and judicial) see themselves as free to extend extraterritorial authority in trade and other matters.

• Convergence of Typical Labor Standards

One approach to the convergence of typical labor standards is to look at pay, as Erickson and Mitchell did, and note the statistical convergence that has been evident among developed countries. In 1960, the U.S. was the highest wage country in the world. After several decades of trade and development, Japan and Europe essentially caught up and the U.S. now has a mid-range position among the high-paying countries. The four Asian tiger countries also have shown wages rising toward developed nation levels. The financial meltdown in Asia may undo some of this progress but the crisis may eventually appear as a brief interruption in a long-term trend toward catching up. However, wage catch-up is not a universal phenomenon. Mexico has not shown signs of catching up in wages with the U.S. or Canada, despite its membership in NAFTA. And it is not clear whether rapid economic growth in China is raising its very low wage levels relative to its trade partners.

Most of the papers that addressed the issue of wage determination in Forum 5 did so in the context of international collective bargaining rather than more general pay setting. For example, Blyton and co-authors study the impact of international airline de-regulation on collective bargaining. Under the old regime in the airline industry, international carriers had prices fixed through cartel-type mechanisms. With guaranteed markets, it was possible for them to provide secure jobs at good wages. However, the move to privatize government-owned airlines and allow "open skies" competition is changing the nature of the marketplace. The price of airlines and fuel is much the same to all carriers. Thus, the authors report, labor costs become a major element of competition under the new regime.

Visser sees the issue of wage bargaining as extending beyond a single industry. More and more countries are competing in interna-



tional markets with the collapse of communism in Europe and the shift in trade policies in emerging nations. It is usually assumed that unions are advantaged when they face relatively inelastic demand curves for labor. However, labor demand becomes more elastic as more and more substitutes become available. Thus, union bargaining positions are being eroded, at least in industries producing tradable goods and services. In the long run, Visser asks, can there be collective representation of employees under these circumstances?

In some cases, unions hope to use contacts abroad to increase their bargaining leverage with MNCs. Russo's paper tells the story - still incomplete - of a Teamsters union campaign against a Dutch holding company, Royal Ahold NV. This MNC is the owner of a retail food chain (Tops) in Buffalo, New York (U.S.A.). Tops has been implementing various innovations in its warehousing and delivery system. Those changes potentially had an adverse impact on Teamster truck drivers employed by food suppliers to Tops. Since the delivery drivers were not Tops employees, Tops refused to negotiate with the union about them. Through an international trade secretariat and other contacts abroad, the union was able to start negotiations. However, no accord was reached and the story continues to unfold. Thus, it is unclear whether the eventual outcome will be an illustration of successful international bargaining or, alternatively, an example of why such bargaining is so difficult.

• Convergence of Mechanisms of Employee Participation

As part of the economic and political integration of the EU countries, various social clauses are being implemented. These include provisions for European works councils within MNCs. Koch sees these relatively new councils as being possible forums for international collective bargaining. However, he notes, the councils are functioning against the backdrop of high unemployment, partly the result of the drive to meet the Maastricht criteria for a single European currency. What may emerge from the councils is still unknown. Simply having a mandatory council is not necessarily the same thing as having strong bargaining power. Indeed, Koch points out, some councils in France and Germany have been the scene of concession bargaining in which worker benefits have been lost. Such results are similar to the union concession bargaining which developed in the U.S. during the 1980s.

In any event, it is not obvious what impact a formal, mandated council will have on actual workplace outcomes. Grytli and Olsen



suggest that mere legal requirements that worker representatives and managers meet in a forum do not necessarily produce results. In Norway, unions have found that if they want to turn such meetings into venues where workplace outcomes are influenced, they will need to back up the formal system. The formal system must be supported by informal union contacts with management counterparts. Similarly, if unions want to coordinate with labor groups in other countries, they will need to develop informal relations with those groups as well.

Marginson sees a "Eurocompany" emerging, different - presumably - from MNCs based outside Europe. The Eurocompany may be state-owned, family-owned, or shareholder-owned and may operate outside its home country. But because of the development of the single market with a single currency, and the rise of EU-wide social directives, it will operate in a similar fashion wherever in Europe it is found. The European works councils will be one element, he believes, characterizing the Eurocompany. Along with related international collective bargaining, works councils will be part of a European convergence.

Jensen and co-authors see three regimes developing in advanced economies. One is a European approach with works councils and international collective bargaining. However, the authors see competition within the single market as a threat to the social partner approach. A second is a U.S. model with de-unionization and, where unions exist, a mix of adversarialism in some cases and "partnership agreements" in others. A third is a Japanese model with some unionization, but of a more co-opted variety.

The reference in a few of these papers to the single market with a single currency points to the macro side of the convergence issue. Unfortunately, as noted earlier, I find this important matter insufficiently discussed in Forum 5 papers, especially those dealing with Europe. There are important ramifications of the move to a single currency in particular. I will use the prerogative of the rapporteur to discuss this neglected topic further in the next section.

Macro Considerations

The concern among European contributors to Forum 5 is that global competition is eroding the old model of employee protection and social insurance that has been developed since World War II. In particular, it is feared that the demand for more employer "flexibi-



lity" is undermining mandated job security guarantees. And - so this thinking goes - competition over costs is leading to a "race to the bottom" during which social charges will be slashed.

- Income or Job Security?

It is important in any discussion of protecting workers to define what it is that one wants to protect. Presumably, job security is simply an instrument to produce income security. But these two targets of protection are not identical. Under certain circumstances, mandated job security for some workers can produce income insecurity for others. And under different circumstances, it is possible to have income security without job security.

Consider a period of economic sluggishness and high unemployment. Within that context, governments can mandate protections for those who already have jobs. But giving these "insiders" a lock on their jobs tends to make job search more difficult for "outsiders" looking for work. The outsiders will often be young, new entrants to the workforce. Job and income security for existing employees can thus produce income insecurity for job seekers.

Alternatively, consider a full-employment economy with labor shortages. Even within such an economy, there may be layoffs as individual firms experience drops in demand for their products. But any laid-off workers are simply sucked up by other employers into new jobs. In such situations, although there may not be job security, there is market-based income security. The security comes from the knowledge that there is always another job.

In the U.S. during the past couple of years, there have been many reports of labor shortages. Unfortunately, we have no official American survey of unfilled job vacancies. However, as co-director of UCLA Anderson Business Forecast Project, I keep track of reports in the press of asserted labor shortages through a computerized database. These reports have become more and more frequent in recent years, in concert with falling unemployment rates. Many of the press accounts tell of employer strategies for enticing workers. The articles refer to employers paying signing bonuses to new employees or paying bonuses to existing employees who recruit their friends. They tell of employers offering training and other benefits as attractions to potential recruits. And they tell of employer groups pressing Congress to relax immigration restrictions to allow hiring from abroad. The occupations involved range from



high-tech computer engineers and programmers to skilled blue collar workers and even to unskilled hotel and restaurant workers.

- Barriers to Mobility

In the American context, however, there is an institutional problem for workers, even in such a high-pressure economy. Because public social insurance arrangements are more limited than in Europe, workers' pensions and health insurance are generally tied to their jobs. And there are often problems in the portability of these benefits. A job change could mean loss of health insurance, for example, although recent legislative changes have aimed at easing this problem. Under traditional defined-benefit pension plans, moving from one employer to another can also be disadvantageous in the U.S., especially for mid-career and older workers.

As Jacques Rojot and I pointed out several years ago, European social insurance tends to be more portable than are American employer-based private benefits. In Europe, social benefits are often provided by government or quasi-government entities external to individual employers. A job change, therefore, does not mean an entitlement loss. We thus have a paradox. In the U.S., where mobility tends to be higher than in Europe, institutional arrangements concerning social benefits hinder mobility. And in Europe, where mobility is relatively low compared with the U.S., benefits are arranged as if to foster mobility. We need not go into the historical accidents that produced this anomaly. But the bottom line is that if European countries could achieve American-style full employment, they could have income security without so much concern about job security. So the issue that must be addressed is the ability of European countries to return to full employment. Can they follow full-employment policies?

- Implications of the Single Currency

When the issue is what policies might be taken to lower unemployment, the standard answer of economists is "monetary and fiscal." Of course, there are other policies that might also be cited. But without monetary and fiscal policy, countries are lacking very important macroeconomic instruments.

The planned move to a single currency issued by a single central bank in Europe will remove monetary policy from the control of



any one participating country. It might appear that such countries will at least have fiscal policy remaining at their disposal. But what remains of fiscal policy under such conditions will be very limited. Why do I make such an assertion? I make it from direct experience.

- The California Example

As it happens, I come from an economy containing 32 million people with a per capita income slightly above the U.S. national average. That economy belongs to the State of California. And as its boosters like to point out, if California were a country, it would rank about 8th among other nations of the world in terms of its gross product. But, of course, California is not a country. It has no currency of its own. Monetary policy is made for California by a central bank whose authorities meet in Washington, D.C., three time zones to the east. California has no special influence over those authorities, despite the critical nature of their decisions for its economy.

Chart 1 plots the annual change in nonfarm employment in California against nonfarm employment in the rest of the U.S. If the two lines appear correlated, it is because they are tightly locked together by internal trade and investment. The U.S. business cycle essentially dictates the California business cycle. Deviations can occur in California. But since 1940, those deviations have largely been functions of military spending. Wars, including the Cold War, have stimulated the California economy because of the state's concentration of aerospace production, especially in the Los Angeles area. Cuts in military spending, on the other hand, have historically had a disproportionately negative effect on California's economy.

The California state government, of course, takes in tax revenue and spends its funds. In that sense, the state has a fiscal policy. Indeed, the state's annual consolidated budget runs about \$70 billion at present. But how independent is California in conducting its fiscal affairs? More particularly, what can state government do to stimulate the California economy during periods of high unemployment? The answer is, "not very much".

Indeed, there is a history of tacit recognition of the state's fiscal impotence. In the 1930s during the Great Depression, various colorful populist social and political movements arose in California. They went under such names as EPIC (for "End Poverty in California"), the Utopian Society, and "Ham and Eggs for

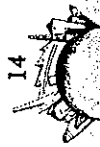
Californians" and they roiled state politics for several years. A common theme among these interconnected movements was that California should create some kind of state currency to finance additional stimulatory expenditures. Odd as these movements were, their founders had grasped a fundamental truth. Absent its own monetary policy, there was little California could do to get itself out of the Great Depression.

However, it is not necessary to reach so far back into history to see what it means for a large economy such as California's to have no monetary policy. Nor is it necessary to focus on so dramatic an episode as the Great Depression. In 1990-1991, the U.S. economy suffered a brief and mild recession. Not surprisingly, the California economy turned down at the same time. But the California economy also was hit by the end of the Cold War. Chart 2 shows the marked decline in real U.S. defense spending after 1987. Chart 3 shows the fall in aerospace employment in California that resulted. The compounding of the U.S. recession and the aerospace shock set in motion a major recession in California, far deeper and more prolonged than that of the rest of the country.

Home prices tumbled in the state, an asset deflation-for-California residents that reduced personal consumption and compounded the recession. And, of course, California unemployment rose well above the U.S. average. One does not have to be an economic determinist to see a connection between these developments and the 1992 Los Angeles riots.

While the U.S. level of nonfarm payroll employment regained its previous peak in 1993, California did not get back to its prior employment peak until late 1995. And, of course, the labor force had continued to grow during 1990-1995 so that unemployment remained high even then. As Chart 4 shows, the California slump left a permanent mark on the state. Compared to the previous growth path, 2.4 million nonfarm jobs were permanently "lost" to the state. So the question naturally arises, what did the state government do about the California recession, given the fiscal resources it had? The answer is that the state government followed anti-Keynesian policies, raising taxes and cutting expenditures. In short, state fiscal policy aggravated the recession; it did not resist it.

Why was such a perverse fiscal policy followed? The answer to that question is simple. The state had no choice. Since there is no California currency and no California central bank, the state government is limited in the budget deficit it can run. Technically, there



are legal requirements that the state balance its projected budget. But it is not the legalities that drive state fiscal policy; it is the bond market. Since California can't create its own currency, it cannot run large deficits without making its securities risky. Lenders demand higher and higher interest rates as state deficits rise to compensate for the risk of default. Eventually, they would refuse to lend at all if the state acted "irresponsibly."

During the California recession of the 1990s, tax revenue to the state naturally declined. Reduced personal incomes cut income tax collections. Reduced profits cut receipts from corporation taxes. Reduced consumption cut sales tax and excise tax revenues. So - in response - California's tax rates were raised and its government expenditures were cut. And much of the expenditure cut fell on social programs.

Realizing that no fiscal or monetary solutions were available, state politicians were nonetheless anxious to do "something" to appease their angry constituents. However, all they could do was to try and improve the state's "business climate" and to try and make the state more "competitive" relative to other states. It was hoped that such actions would encourage investment from the rest of the U.S. and deter California businesses from leaving the state.

In the end, there was much symbolic political action. The state legislature became focused on reducing the cost to employers of the workers' compensation program, a mandatory program of insurance which compensates workers who experience job-related injuries or illness. While the program certainly needed reforms, there was minimal relation between these reforms and state economic performance. For most employers, the change in premiums paid to support the workers' compensation program was too small to affect job creation or retention.

In principle, the state might have made itself more competitive by cutting its wages relative to those of other states. Had California been a separate country with its own currency, it might have deviated to achieve that effect. But the only way such labor cost cutting could have been achieved (absent a monetary system) would have been through reductions in nominal wages in California relative to other states.

Did market forces produce such a relative wage decrease? At the start of the recession in 1990, California's annual and weekly wages were 10% above the national average. By 1996, the state's wage



premium did drop, but only to 9%. That is, there was virtually no relative wage adjustment despite the severity of the California recession. This result is not surprising; empirically-oriented economists have long known that wages are not very responsive to economic slack.

So how did California adjust to its unavoidable job losses? The drop in employment was particularly severe in the manufacturing sector, especially for occupations involving just a high school education or perhaps some college or post-high school training. In simple terms, job losers in those categories eventually left the state to look for jobs elsewhere. California, which had historically experienced net in-migration from domestic and foreign sources shifted to net out-migration, as shown on Chart 5. Foreign immigration slowed and domestic migration became negative, although the state's population continued to grow through natural increase (excess of births over deaths).

Now that the California economy has resumed its upward movement (although on a lower track than before), the migration pattern has reversed. California is again experiencing net in-migration. In short, the adjustment mechanism for California is migration, not wages. During booms, people come to California for jobs. During slumps, they leave.

• A Europe of Californias?

European states who join the European Monetary System are turning themselves into economic Californias. They are surrendering their economic sovereignty. Of course, they will still be countries with flags, postage stamps, and ambassadors. (California, in contrast, has a flag but no postage stamps or ambassadors.) Whether there are more pluses than minuses in that decision is far beyond the scope of this report. Obviously, the states of the U.S. - including California - obtain many benefits from being within a monetary union. So I am not arguing that the EU shouldn't form a monetary union. However, I am arguing that there are implications for labor policy of the EU's move to monetary unity and - as noted earlier - it is surprising that these were not featured in Forum 5.

Note first that the level of mobility in Europe between countries is far less than between California and other states of the U.S. There are obvious language and cultural barriers in Europe that do not exist within the U.S. So the migration safety valve that California enjoys in recessions - if "enjoys" is the right word - does



not exist in Europe to anywhere near the same degree.

Note second that in the U.S., the major labor and social insurance policies are made at the federal level. Social Security is a federal program. Unemployment insurance is administered by the states but its broad outlines and funding mechanisms are largely federal. Occupational safety and health standards are federally set, as is the minimum wage. In some cases states can exceed the federal minimum standards if they wish, but they cannot go below them. Thus, although states may cut social programs and protections during recessions for reasons of "competitiveness" - as California did - there are federal limits to what can be cut.

Although the Europe is moving toward EU-wide social policies, the individual member nations are far more important in this sphere than are the states within the U.S. Social insurance, for example, is not provided at the EU level in Europe. That means that during future recessions, if European states compete to improve their business climates (as California did), the potential for social cuts and reduced job protections is much greater than in the U.S. One has to wonder, for example, about the fate of unfunded or underfunded national social insurance programs as the European baby boom ages. Will bond markets permit large government deficits to maintain such programs?

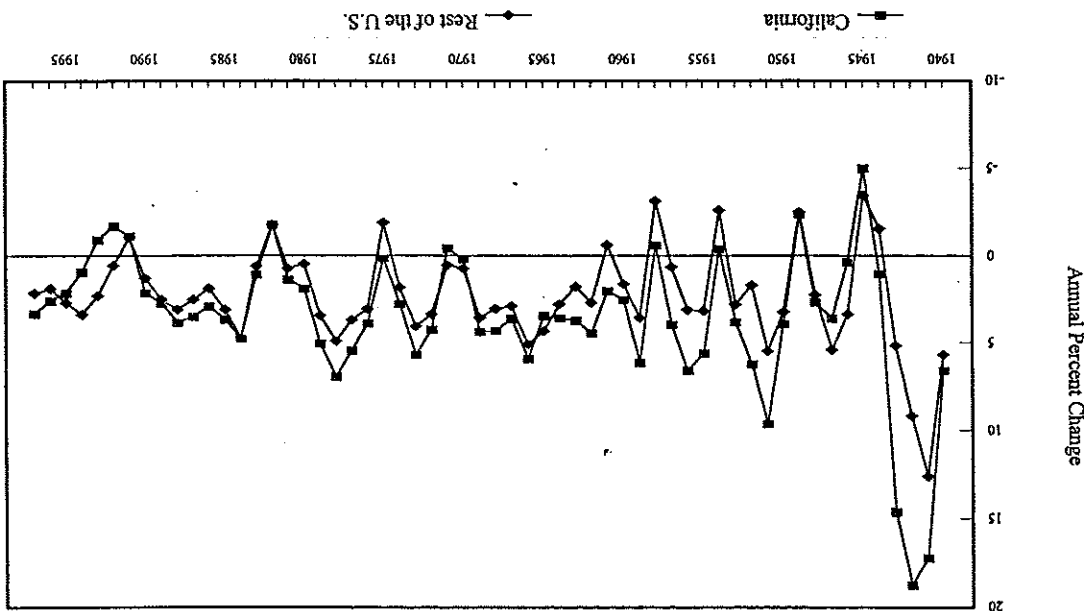
Finally, it should be noted that if the major EU countries become part of a unified monetary system, those countries which remain outside the system may not retain as much autonomy as they expect. Canada, for example, does have its own currency and monetary system. But it is locked into a tight trading relationship with the much larger and unified U.S. economy. Compared with the combined states of the United States, Canada's economy is small. Its gross product is less than two thirds the size of California's. The Canadian business cycle exhibits a somewhat greater degree of independence from the U.S. than does California's. However, it is still the case that Canada's business cycle heavily reflects U.S. economic conditions.

Once much of the EU becomes a large, unified, single-currency economy, the economic autonomy of those nations that choose to remain outside will be limited, just as Canada's autonomy is limited. In short, the EU - whose roots go back to a trade agreement of the 1950s - is now embarked on a profound social experiment. The experiment has important implications for employment practices and social policy. And it may be that other world trade blocs will

eventually consider integration of their monetary systems along EU lines.

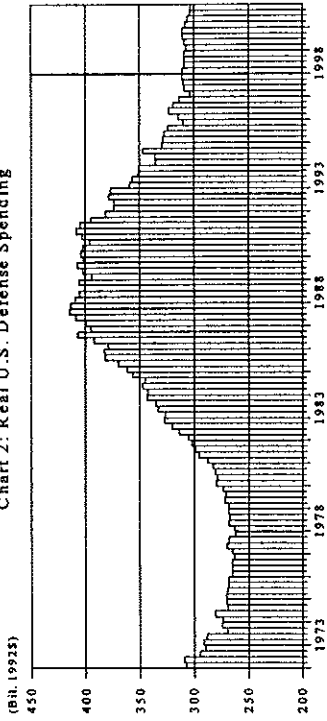
The topic of Forum 5 was "Labour-Management Relations in a Multinational Context: International Trade Agreements and Social Clauses." Yet we did not hear much about the implications of this experiment within the Forum. Happily, the IIRA has chosen to take up the monetary issue in a special seminar at the Bologna conference.² Let us hope that at the next World Congress with more evidence at hand, the topic of monetary union will continue to command our Association's attention. It may turn out that monetary union is a stronger influence on convergence of employment practices and social insurance than trade integration.

Chart 1: Annual Percent Change in Nonfarm Payroll Employment: California and the Rest of the U.S., 1940-1997



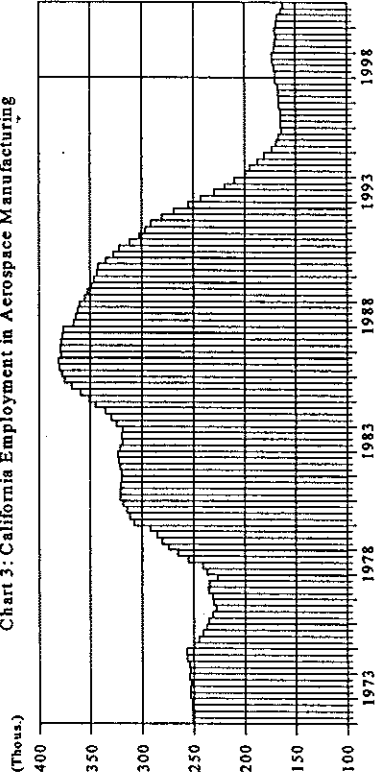
Source: U.S. Bureau of Labor Statistics

Chart 2: Real U.S. Defense Spending



Source: UCLA Anderson Business Forecast, March 1998

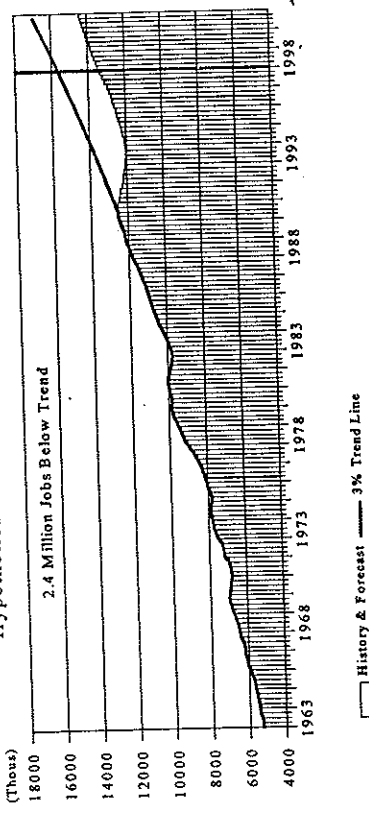
Chart 3: California Employment in Aerospace Manufacturing



Source: UCLA Anderson Business Forecast, March 1998

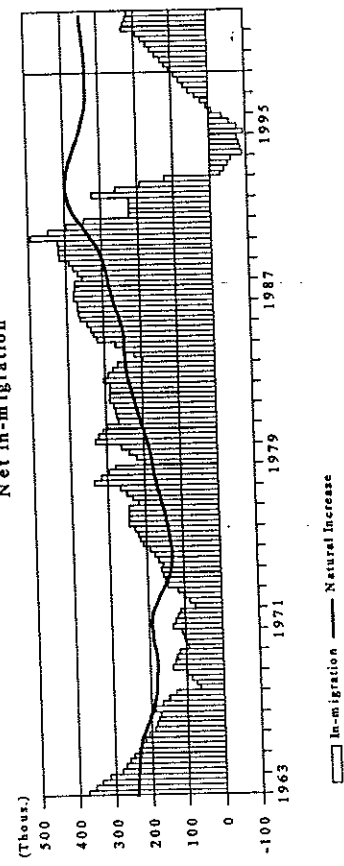


Chart 4: California Nonfarm Employment: Actual and Hypothetical 3% Trend from Third Quarter of 1990



Source: UCLA Anderson Business Forecast, March 1998

Chart 5: California Net Natural Increase and Net In-migration



Source: UCLA Anderson Business Forecast, March 1998

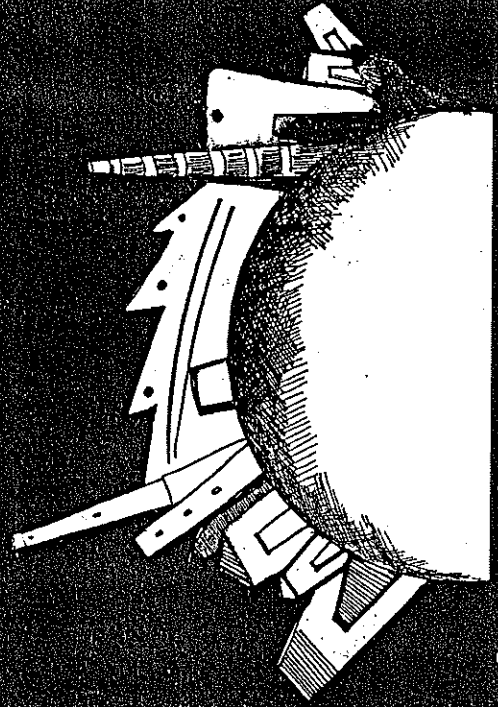


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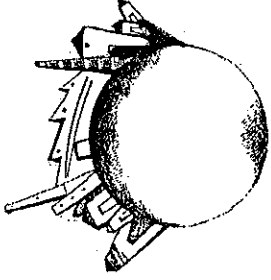


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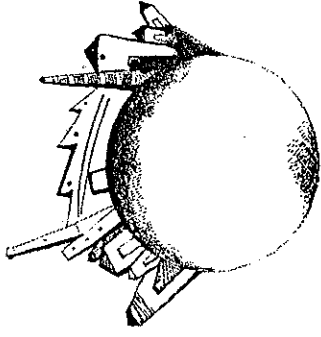
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FORUM 5

BARGAINING GLOBALLY: LABOUR-MANAGEMENT RELATIONS IN A MULTINATIONAL CONTEXT. INTERNATIONAL TRADE AGREEMENTS AND SOCIAL CLAUSES

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