

East European Labor, the Varieties of Capitalism, and the Expansion of the EU

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Comments are welcome

Abstract

With the European Union now expanded to include ten new member states, the transformation of industrial relations in postcommunist eastern Europe has become increasingly important, including for the nature of capitalism in Europe as a whole. Following the varieties of capitalism literature, which divides advanced capitalist economies into coordinated and liberal market models, this paper examines labor institutions in eastern Europe to determine which of the types they most approximate. We then find that, despite the surface similarities of the communist political economy with the coordinated model, nine of the ten postcommunist (new and prospective) member states are much closer to the liberal than the coordinated ideal type. Again following the varieties of capitalism approach, but also guided by criticisms of its perspective on institutional change, we find that the prospect that the eastern European countries will converge or harmonize toward existing European labor and social standards to be unlikely. Rather, it appears more likely that the liberal approach of the new member states will provide a significant additional impetus for the further liberalization of the coordinated economies of western Europe.

In the short time since the European Union (EU) has expanded eastward, considerable fears have arisen in "old" Europe, especially regarding east European labor and the future of the European social model. Because of the uneven nature of the old and new member states in terms of wages and living standards, western European populations have expressed anxiety about the immigration of labor from the east. Pundits have pointed to such fears and the mythical "Polish plumber" to explain the recent French and Dutch rejections of the new European constitution. Still others have argued that the greater threat to western European societies, or more precisely to the European social model which they are said to uniquely share, is "social dumping," or the mobility of capital, attracted by the significantly lower wages and social standards in the new member states of eastern Europe. All of this is said to contribute to the "enlargement fatigue" of western European publics, putting the more ambitious plans for EU expansion into doubt.

Are such anxieties justified? The "varieties of capitalism" argument -- the dominant theoretical approach to the study of advanced capitalist societies -- would suggest they are not. In contrast to simplified notions of economic globalization leading to a "race to the bottom" as countries lower their labor and social standards, the varieties of capitalism framework argues that there are at least two distinct varieties of capitalism -- liberal and coordinated market economies -- and that these types are resistant to global pressures for convergence. Hence, this framework would suggest, the anxieties about liberalizing pressures from the east are overstated.

This paper will argue that the varieties of capitalism framework can be fruitfully applied to the new EU member states of eastern Europe.¹ However, the results of so doing, rather than alleviating anxieties about liberalization pressures from the east, suggest that such concerns may well be warranted. Indeed, the application of the varieties

¹ This paper will focus on the eight postcommunist countries that have joined the EU, and Bulgaria and Romania as likely entrants by 2007, and as a group will be variously referred to here as "east central Europe," "Eastern Europe," or "new member states." Cyprus and Malta will not be discussed further, since they are both quite small and lack the characteristics of postcommunist societies. In terms of the varieties of capitalism, they share some of the liberal attributes of the postcommunist societies, but not all.

framework to eastern Europe also suggests some strengths and limitations of the varieties of capitalism framework itself.

In what follows, we will pursue the varieties of capitalism framework which argues that the advanced capitalist countries can be placed in one of two ideal types: coordinated and liberal market economies. The paper will then argue that this framework can be extended to the new member states of eastern Europe. It will argue further that, once criteria for the two varieties are established, all but one of the new member states are much closer to the liberal than the coordinated model of capitalism. Moreover, following the theories of institutional change invoked by the varieties of capitalism argument, as well as more recent criticisms of it, the likelihood of convergence or harmonization to existing EU norms is called into doubt. Rather, it is more likely, the paper will argue, that the coordinated economies of Europe will be adversely impacted by the liberalism of new member states of east central Europe.

Varieties of Capitalism in Europe

After fifteen years of political and economic transformation, the countries of east central Europe have been transformed from communist dictatorships into capitalist democracies, their achievement symbolized most vividly by their recent membership into the European Union (EU). Yet what sort of capitalism has been created in eastern Europe, particularly regarding labor, which has experienced some of the most wrenching changes during this transformation? What implications might the nature of these new capitalist economies have for the expanded EU?

The now extensive literature on the "varieties of capitalism" can prove useful in answering such questions. The varieties of capitalism theoretical perspective makes two central claims: first, that even in a globalized era, there are distinct national types of capitalism, and second, these varieties of capitalism are largely resistant to change (Hall and Soskice, 2001; Kitschelt, et. al., 1999; Iversen, Pontusson, and Soskice, 2000). As a recent review essay on the topic summarized the view, "something approaching a consensus has now emerged around the notion that national capitalisms are distinguished from one another by particular configurations of ... institutions" and that "these distinct national

capitalisms are quite resistant to pressures toward convergence" (Howell, 2003). Let us look at the implications of each of these arguments in turn.

The varieties of capitalism literature, which has focused until recently on advanced capitalist societies, has categorized the varieties most often as liberal versus coordinated market economies. There are no doubt simplifications in such a dichotomy, even more so if we attempt to stretch these categories to economies that are less advanced.² We risk more simplification if we confine our focus primarily to industrial relations; however, three of the five "spheres" that differentiate firms in each capitalist variety directly impact labor: bargaining mechanisms for wages and work conditions, vocational training, and employee relations generally.³ Thus, in coordinated market economies, one typically finds high levels of union membership, highly articulated mechanisms of social dialogue with well organized employers, resulting in collective agreements with a high rate of coverage at the national or sectoral level. These elements are combined with education and training systems that provide high industry-specific or firm-specific skills, and worker participation or co-determination at the workplace [see table 1]. Conversely, in liberal market economies one finds flexible or decentralized labor markets with low levels of union density, enterprise-level bargaining with limited extension to other workers, and little or poorly-functioning mechanisms of social dialogue with limited employers' coordination across firms. Education tends to focus on general skills to complement the fluid labor markets, and there is a high degree of managerial prerogative with little to no co-determination in the workplace (Thelen, 2001; Howell; Feldmann, 2006).

[table 1 here]

Moreover, if we confine our discussion to industrial relations, the central elements of the coordinated variety of capitalism overlap with what has been called the European social model. This is not surprising, since according to the institutional logic and the complementary nature of the different spheres in the varieties of capitalism framework, "there should be a correspondence between types of political economies and types of

² Hall and Soskice note that some countries, such as France, Italy, and Spain, don't easily fit into either ideal type, and suggest a possible "Mediterranean" type (Hall and Soskice, 2001).

³ The other "spheres" that won't be addressed here are systems of corporate finance and inter-firm relations (Hall and Soskice, 2001, 6-7).

welfare states" (Hall and Soskice, 50-51). There is much conflict in the EU itself, between countries and social groups, on the extent to which this social model is a desirable goal. Still, there is much declarative policy at least that the EU is not only an economic but also a political and a social project, such that the European social model represents a set of institutions that makes European capitalism distinct, and for some, an important counter to American-style globalization. The elements in this model include the "vision of the European member states as 'welfare states,' the recognition of social rights and the role of social partners, the existence of public services and the social protection systems" (Andre, 2002). Other elements are said to include universal social protection as opposed to a targeted "safety net," minimum labor standards, and strong social dialogue and workers' participation (Vaughan-Whitehead, 2003). Several of these elements are enshrined in various EU charters.

The second theoretical thrust of the varieties of capitalism literature is based firmly in institutional theory, and emphasizes that these varieties of capitalism – and the coordinated market economies in particular -- are a product of a specific historical trajectory and resistant to change. In most formulations of institutional theory, institutions are seen, almost by definition, as sticky and resilient. The notion of path dependence in particular looms large in the discussions of varieties of capitalism, whereby "particular courses of action, once introduced, can be almost impossible to reverse; and consequently, political development is punctuated by critical moments or junctures that shape the basic contours of social life" (Pierson, 2000). Thus other than certain critical junctures that create moments of institutional openness, institutional arrangements are shaped by lock-in effects and paths of increasing returns (Pierson, 2000; Howell, 2003; Hall and Soskice, 2001) . Thus, even with the liberalization pressures posed by the current phase of globalization, coordinated market economies will not necessarily, or even likely, converge to the liberal model.

More recently, critics have challenged this "punctuated equilibrium" model of institutional change employed by the varieties of capitalism framework. In particular, liberalization can occur in ways that are at the same time incremental and transformative, leading to "gradual transformative change" (Streeck and Thelen, 2005, p 2). Such incremental institutional change may be particularly suited towards liberalization (rather

than in the direction of coordination), since, in contrast to non-liberal reforms, liberalization "can often proceed without political mobilization," in part because liberalization faces fewer collective action problems, and liberalizing trends can be brought about by individual exit rather than collective voice (Streeck and Thelen, 2005, p. 33). That change in a coordinated direction faces greater obstacles is underscored by a recent study of "the origins of nonliberal capitalism" which finds that nonmarket coordination is typically the product of historically contingent conditions and especially difficult to construct (Streeck and Yamamura, 2001; Crouch, 1993; Howell, 2003). In this way coordination might be particularly path dependent, since, for example, elements of coordination can be traced back to pension reforms carried out by Bismark in the nineteenth century.

The historically contingent nature of coordination is illustrated in an example central to our discussion of labor: namely, the way that social dialogue, or corporatist institutions, evolved in western Europe. In the postwar era, corporatist bargaining was the mechanism for maintaining policies of full employment, which unions accepted in exchange for wage restraint; strong corporatist institutions were said to explain low strike rates in certain western European countries (Schmitter, 1981; Cameron, 1984). In his study of "industrial relations and European state traditions" Crouch underscores that while labor peace coincided with strong corporatist systems in the postwar era, corporatist institutions evolved historically as a response to high levels of labor unrest in Scandinavia and elsewhere. "As conflict became significant, employers and governments sought to construct institutions that might contain it; elsewhere, workers ability to disrupt was too sporadic for employers to bother" (Crouch, 1993, p. 99). Thus, employers organized themselves only once labor had prodded them to do so. While some more recent work in the varieties of capitalism literature argues against this "labor mobilization" view for the coordinated variety of capitalism generally, it does so by stressing the importance of employers' organizations in the historical emergence and continued resilience of coordinated market economies. If this were the case, then if not strong labor organization a society would need strong employers' organization to bring about social dialogue of the coordinated variety.

This brief discussion of the varieties of capitalism argument raises clear concerns about the longer-term consequences of EU expansion, which is ostensibly based on the goals of economic convergence and social harmonization. Here the varieties of capitalism argument points to two significant problems. First, as we shall see, new member states are much closer to the liberal than the coordinated variety of capitalism. Second, to the extent this is true, even if the more optimistic scenarios for the economic convergence of new member states toward EU levels were to be realized, the hoped-for convergence toward a coordinated market economy would be much less likely, indeed quite difficult to bring about. Let us address each of these problems in turn.

What Type of Capitalism in East-Central Europe?

Before we investigate the current form of labor relations in east central Europe, let us recall that just fifteen years ago, these societies were quite easy to characterize as a specific regime type, namely communist. In terms of industrial relations, if ever labor markets anywhere could be termed "rigid," it was here.⁴ These countries each had near-universal union membership, with wide-spread and compulsory collective agreements, though rendered almost meaningless by the central-setting of wages by planners. Planned wages were circumvented to a certain extent through shop-floor bargaining, which was strengthened on workers' side by an often significant labor shortage. Partly owing to that shortage, and to the ideological privilege of labor in communist societies, while wages were low, the social benefits obtained through the workplace were often significant, labor laws were quite generous in comparative terms, and there were at least formal means of workers' participation in several countries. Inequality was low, and with the exception of Yugoslavia, formal unemployment was unknown. However, since so much of the structure of labor relations was determined unilaterally by the Communist Party, with the

⁴ If communist political economies could be placed at the opposite end of liberal economies on a continuum measuring flexibility, this does not mean they were akin to coordinated market economies, if for no other reason than they were not market economies of any variety, nor were they characterized by coordination among private actors, but rather by state direction. Nevertheless, they had at least a surface similarity with certain elements of coordinated markets, many of which were dismantled through liberalization.

officially-recognized trade unions subordinate to the Party, assertive labor movements arose in some places, most notably in Poland where the Solidarity movement played a central role in ending Communist Party rule. Given this apparent labor assertiveness, with the end of communism and the introduction of capitalism, scholars and policy makers alike predicted that labor would mobilize to defend its prerogatives.

Union Density

What is the situation in the region today? Perhaps the most basic measure of labor's strength, and an important dimension on which liberal and coordinated market economies are said to differ, is the rate of union membership, or density (Golden, Wallerstein and Lange, 1999). Since union membership was nearly compulsory in many communist societies, it is not surprising that membership rates have dropped considerably, and by some accounts are now converging with western European levels. A World Bank publication from 2002 cites average union density figures for the then-EU accession countries that are above the averages for EU and OECD countries (Riboud, Sanchez-Paramo, and Silva-Jauregui, 2002). This would place the postcommunist countries within the range of coordinated economies.

However, more recent figures suggest that union density in the region has declined more steeply: union density in the new EU member states is generally well below that of the old member states, at 24.6% on average for the new member states, and 38.2% on average for old members (Visser, 2004; Lado, 2002).

[figure 1 about here]

However, two qualifications need to be added. On the one hand, the western European average is high primarily because of the few countries that use the ghent system of unemployment insurance (Rothstein, 2002); without these cases, the old and new member states look much more comparable. On the other hand, the rate of decline in union membership has been much greater in the new member states, which, despite starting from much higher union membership rates, have within a few years reached

density rates that are on average lower than their west European counterparts (figure 2 here).⁵ While one should perhaps use caution in extrapolating this trend, were it to continue, rather than converging to west European (coordinated) norms, post-communist countries would be clearly headed towards Anglo-American (liberal) levels of union density.

[figure 2 about here]

Collective Bargaining

Union density, however, is an imperfect indicator of labor strength. Coverage laws mean that in some countries collective bargaining agreements extend far beyond union members, as is in France. Hence collective bargaining coverage rates, the level on which those agreements are reached, and the quality of collective agreements are central to the distinction between coordinated and liberal capitalisms. Other things being equal, “substantial declines in union coverage would indicate an erosion of the ability of trade unions to influence wage levels” (Golden, Wallerstein and Lange, 1999, p. 202).

As we have noted, collective agreements were virtually compulsory if fairly meaningless in the communist period. Yet, even more so than with the union density data, the coverage rate for collective agreements in the region has declined well below the EU norm, into the liberal range [see figure 3] (Visser, 2004; Schulten, 2005). Slovenia, at nearly 100%, is a clear outlier here, and we will return to this point. Except for Slovenia, no other east European country has a higher coverage rate than the UK, the lowest in western Europe by this data, and five eastern European countries are lower than the UK. If we exclude Slovenia, the average coverage rate for eastern European average is 28%. The average coverage rate for old EU members (plus Norway) is 75%.⁶

[figure 3 here]

However, the quantity of collective bargaining coverage can appear misleading with probing the quality of collective agreements. Central to explaining the quality of collective bargaining, as well as to the definitions of coordinated and liberal economies,

⁵ Unlike in figure 1, the data in figure 2 are weighted averages, and include some different countries (Visser, 2004).

⁶ Data for Portugal and Luxembourg were missing (Visser, 2004; Lado, 2002).

is the level on which collective bargaining takes place. Again, in coordinated economies, the dominant bargaining level is the national or sectoral level; for liberal economies, it is on the level of the firm. A recent study of collective bargaining trends in Europe found that, of fourteen west European countries, three were dominant at the "intersectoral" level, nine at the sectoral level, one (France) had no dominant level, and only one (U.K.) was dominant at the company level [see table 2]. As for postcommunist countries, Slovenia was dominant at the intersectoral level, Bulgaria and Slovakia were said to have sectoral-level dominance, while seven out of ten were dominant at firm-level (Schulten, 2005). Others have developed a more quantitative approach, called the "centralization of wage bargaining index," which measures the degree of centralization in bargaining on a scale for 1 (fully centralized) to 0 (no centralization). By this measure, the degree of centralization in bargaining is .46 in western Europe, and .28 in eastern Europe [see figure 4] (Visser, 2004).

[table 2 about here]

[figure 4 about here]

The content of collective agreements suggests still more differences with the coordinated model of capitalism. One study finds that collective agreements in eastern Europe "do not address the most crucial aspects of working conditions," and that "wage levels and nominal increases remain the main – and nearly the only – issue described in collective agreements" (Vaughan-Whitehead, 2003, pp. 99, 100). Case studies in the Czech Republic for example have found that even pay is not always covered (Weber, 1997; Pollert, 2001). A survey study of collective bargaining in Hungary found that "many company agreements are far from being real negotiated agreements, but are either defined unilaterally by employers or, following state socialist traditions, simply repeat the law." Further still, in 37% of the surveyed collective agreements in Hungary, there was no stipulation for wages (Neumann, 2002).

Thus, even more so than with union density, in terms of collective bargaining most new member states would appear to be much closer to the liberal than the coordinated model. Slovenia, with near universal coverage and intersectoral bargaining, is a clear exception. Slovakia, with the next highest level of centralization in wage bargaining might appear to be an exception as well. However, one study finds that "while in

quantitative terms Slovakian bargaining practice at the sectoral level is rather impressive, in qualitative terms serious doubts could be raised," while another study argues that the sectoral agreements in Slovakia "remain very general, all issue relevant for workers being discussed and negotiated at enterprise level" (Lado, 2002; Vaughan-Whitehead, 2003, pp. 245-6). Given this, it would appear safe to conclude that along this measure, Slovenia is a coordinated market economy, while the remaining postcommunist states are liberal.

Social Dialogue and Employers

In coordinated market economies at least, collective bargaining takes place through mechanisms of social dialogue or corporatism, though social dialogue often extends beyond collective bargaining to include such issues as employment and social policies. Social dialogue is central to the European social model, and is encouraged by the Maastricht social protocol (Ross and Martin, 1999, p. 371; Andre, 318).⁷ Indeed, some have argued that the future of "Social Europe" rests to a considerable extent on the quality of interest representation among its new entrants (Iankova and Turner, 2000). Post-communist societies explicitly sought to build corporatist institutions, partly spurred by the International Labor Organization and partly because of their strong desire to "join Europe" (Ost, 2000, p. 504).

Several commentators have argued that tripartism has contributed to labor peace in the region, at least in the early transition years (Iankova, 2002; 1998; Hethy, 1994). However, the large majority of the studies of post-communist corporatism have found these institutions to be rather weak and ineffective (Ost, 2000; Crowley and Ost, 2001; Kubicek, 1999; Thirkell, Petkov, and Vickerstaff; Heinisch, 1998). Once again, Slovenia remains a striking exception.

A full discussion of the attempts at social dialogue in east central Europe would require a paper in itself. However, there are reasons for further pessimism about the corporatist experiment in eastern Europe. One reason is that labor in eastern Europe –

⁷ While in many cases these bargains have become seriously frayed in an era of high unemployment, by a number of accounts corporatist negotiations still remain crucial both for bargaining over wages and over social welfare policies.

despite the legacy of Solidarity, the wrenching economic transformation, and the weakness of collective bargaining -- has not displayed sufficient mobilization power in the postcommunist era to compel employers to construct significant institutions of interest intermediation. According to Crouch, "Employers need to engage in a bargaining exchange beyond the simple contract only when labor has developed effective power" (Crouch, 1993, pp. 56; 62-63). As Martin and Ross argue, "The classic incentive bringing employers to the bargaining table is the capacity of unions to disrupt and regulate production by mobilizing their members to strike" (1999, p. 341).

However, when we examine strike rates, measured by the number of workers involved in labor disputes relative to the total number of workers employed, we find a wide divergence of strikes rates in western Europe, with an unweighted average strike rate for these west European countries of 100 days not worked per thousand workers per year. The comparable figure for east European countries is 21.5.⁸

One might argue, on the other hand, that corporatist institutions themselves might explain the low strike rates in east central Europe, just as they have been used to explain low strike rates in certain western European countries. However, our earlier discussion of the historical evolution of these institutions in western Europe revealed that while labor peace coincided with strong corporatist systems and strong unions in the postwar era, corporatist institutions originally evolved in response to high levels of labor unrest in Scandinavia and elsewhere (Crouch, 1993).

Again, more recent work in the varieties of capitalism literature argues that rather than labor, it has been capital, through employer organizations, that was central to the creation and continued viability of coordinated market economies. Still, whether capital organizes on its own, or only in response to mobilization by labor, strong employers' organizations are essential for social dialogue and also to the definition of the coordinated variety of capitalism. Yet, in postcommunist societies, the lack of strong employer organizations has been, in the words of one study, "the most significant weakness in industrial relations since the beginning of the transition" (Vaughan-Whitehead, 2003, p.

⁸ The figures for some Western Europe countries are from 1989-1998, while the rest are from 1992-2001, though data are missing for some countries in some years (International Labor Organization, 2002; Davies, 2000).

259). In contrast to western Europe, where social dialogue evolved through the mutual interest of the social partners, in east central Europe the state, together with trade unions, has tried to push reluctant employers to organize, though with only partial success.

Quantitative data on this question are limited, but with the remarkable exception once again of Slovenia and in this case of Slovakia, in the three other cases with available data the organization rate for employers is even lower than in the UK [see figure 5] (Visser, 2004). In Slovenia, membership by employers in the Chamber of Commerce is obligatory, and the Chamber itself is legally compelled to engage in collective bargaining. While the rate of employer organization in Slovakia also appears high, as with collective bargaining, qualitative studies focused on the issue have questioned the strength of social dialogue in Slovakia (Stein, 2001; Ost, 2000; Bohle and Greskovits, 2005). In other countries, the qualitative evidence suggests the rate of employer organization is likely relatively low, and even if not numerically low, employer organizations are weak.

[figure 5 about here]

As a result this overall weakness of employers as an organized interest, the state has dominated the creation and maintenance of social dialogue in the region, making it more tripartite than bipartite, with a formalistic and legalistic quality as opposed to evolutionary coordination. Even when meaningful agreements are reached on the national level, because of the employers' lack of interest and organization, as well as the weakness of trade unions, there are few means to ensure that the agreements will be implemented at the workplace (Vaughan-Whitehead, 2003).

The lack of strong employer organizations in eastern Europe can partly be explained by the impact of the communist period, where, to put it mildly, private employers were few and hardly organized. Yet, contrary to the recent stream in the varieties of capitalism literature that questions the centrality of labor in creating coordinated market economies, fifteen years after communism and in now privatized economies, the lack of coordination among employers in the region appears to be largely a reflection of the weakness of labor, since employers' have little need to coordinate their

activities without labor compelling them to begin the process.⁹ Whatever the explanation, with the exception of Slovenia, both employers' organizations and social dialogue institutions, while existent, appear to lack a genuine coordination function. While one might argue that the mere existence of social dialogue institutions makes the postcommunist countries distinct from the liberal model, their formal nature and the lack of significant coordination through social dialogue again places these societies closer to the liberal than the coordinated market economies.

Vocational Training

Vocational training is closely related to the strength of employer organizations, since in a coordinated economy, strong employer organizations are needed to prevent the poaching by other firms of workers who have, through apprenticeship, received industry-specific or firm-specific skills. The long-term employment patterns and high unemployment benefits of coordinated economies said to lessen the risk workers might face in acquiring highly-specific skills. In contrast, in liberal economies, with much less cooperation between employers, training tends to take place in formal educational institutions which provide the general skills needed by workers facing flexible labor markets and uncertain employment patterns. A lack of skilled workers can result.

Communist political economies tended to produce skilled labor, and the presence of skilled labor is often said to be one of the comparative advantages enjoyed by postcommunist societies. However, skills training in the communist period was provided not through apprenticeships coordinated by private employers, but in state-run vocational institutions. Moreover, much of the skills training that took place was specific to meeting the demands of a planned economy, not to allowing firms to compete in a competitive global market. We have rather less empirical evidence of the mechanisms of skills training in the postcommunist societies than of the other elements of capitalist varieties examined here. However, we should not be surprised to learn that "in the decade since unification, eastern German firms overall have not invested in apprenticeship training at

⁹ "Employers' organizations were formed during a period of ... the timidity or even political weakness of trade unions" (Lado, 2002, citing Draus).

levels that constitute anything like a high-skills equilibrium" (Culpepper, 2001). This was despite the fact that, in contrast to other communist economies, the GDR "enjoyed an established practice of industrial apprenticeship" based in part on the historical roots of apprenticeship training in pre-war Germany. Eastern Germany also enjoyed an advantage over other postcommunist countries, in that employers' organizations and trade unions were transferred from west to east. Despite these advantages, eastern Germany lacked an uninterrupted tradition of "decentralized cooperation" among private employers to produce the skills needed by competitive firms, making the attempt to transplant the western Germany practice of skills training only partly successful (Culpepper, 2001).

Elsewhere in eastern Europe, foreign firms have shown some interest in skills training to increase productivity and thus the profitability to be gained from relatively low wages. However, as in other spheres, employers, whether foreign or domestic, have shown little interest in coordinating their efforts. As a result, there is an "emerging skills mismatch in the labor market" in east central Europe, and the education system is not training the right kind of workers.¹⁰ This is precisely the type of shortcoming the coordinated model of skills training is designed to alleviate. While the evidence in this sphere is more limited, there is little sign that the new member states of eastern Europe are adopting the coordinated model of skills training.¹¹

Workplace participation

In addition to mechanisms for participation and articulation of interests at the national and sectoral level, coordinated market economies typically have institutions for worker participation at the level of the firm. In the coordinated model, mechanisms such as co-determination boards help facilitate cooperation and information sharing among employers and employees, which, together with expectations of stable or long-term employment, are tied to the development of firm-specific skills, all of which, it is argued, improves the competitiveness of coordinated firm. Workers' participation is also a central

¹⁰ "East European Economies: East, West and the Gap Between," *The Economist*, Nov. 26, 2005, 63-64.

¹¹ Consistent with the argument in this paper, we might hypothesize however that Slovenia would be closest to the coordinated model of skills training.

element of the European social model, and works councils exist most EU states (Vaughan-Whitehead, 2003, p. 276). Moreover, "Information and consultation rights for workers are a key element of the 'acquis'" which all new member states were compelled to adopt as a condition of EU membership (Lado, 2002). At the transnational level, European Work Councils seek to coordinate the participation of employees working for the same multinational corporation in different countries.

In the communist period, several eastern European countries had worker councils, although, as with collective bargaining, these were often quite formal in nature. However, by 2000 only Hungary and Slovenia retained works councils or other means of representation beyond unions, though new legislation in the Czech Republic and Slovakia sought to create such institutions. With the exception once again of Slovenia, where, as in Germany, unions see works councils as an additional avenue for worker input, trade unions in the region have been critical of works councils as a means for employers to undermine unions (Vaughan-Whitehead, 2003, pp. 286-293). Moreover, while most west European multinationals operating in east central Europe have established European work councils, very few of them have any worker representatives from the region, thus making them incapable of performing their stated function -- to share information between employees working for the same firm in different countries (Vaughan-Whitehead, 2003, pp. 294-5). Contrary to the intention of these institutions, trade unions from the host countries appear to be resisting the addition of representatives from east central Europe, leading to "a tacit agreement between workers and managers in the host country to impose some agreements on east European workers" (Vaughan-Whitehead, 2003, p. 297). Overall, workplace participation appears like the other measures we have looked at: with the exception of Slovenia (and in this case, perhaps Hungary), the postcommunist countries appear closer to the liberal than the coordinated model.

Additional measures of liberalization

We have now seen a number of indications of the liberal nature of labor relations in postcommunist societies. Other measures, while not explicitly part of the varieties of capitalism framework, might help us either confirm or question this finding. We would,

for example, expect to find flexible labor markets in a liberal economy. A study of “twenty engines of growth for European transition countries” published by the World Economic Forum and Harvard’s Center for International Development found that while the transition countries lagged on almost all of the twenty indicators, the main exception was “labor market flexibility,” as measured by a survey of executive opinion. The survey probed the degree to which hiring and firing was determined by regulations or employers, the extent to which hours were flexible, and the degree of decentralized wage setting. On a scale of 1-7, labor flexibility for the EU on average was 2.9; for postcommunist societies the average was 4.6.¹² Slovenia was the only postcommunist country below the EU average.

We would also expect to find greater inequality in liberal economies, since the wage bargaining system, the stronger unions, and the skills training system associated with coordinated economies are strongly correlated with lower levels of inequality (Rueda and Pontusson, 2000; Estevez-Abe, Iversen, and Soskice, 2001, p. 177; Ross and Martin, 1999). As pointed out above, during the Communist period economic inequality was quite low. We would certainly expect greater inequality with the introduction of capitalism, and thus already by 1994 average Gini coefficients for East Central Europe were 27, close to the OECD mean (Ringold, 1999). However, by 1998, less than a decade into the transition, only the Czech Republic was at the EU average of 25.9, and the region's average Gini coefficient, at 31.9, was close to the averages of the U.K. (32.4) and the U.S. (34.4).¹³

What might the level of unemployment tell us about the type of capitalism that has been created in east central Europe? High unemployment levels have bedeviled a number of core EU members in recent years. Yet while unemployment was virtually unknown in the communist period, the average levels of unemployment in the postcommunist region are higher, largely due to exceptionally high levels in Poland and

¹² This postcommunist average includes some non-candidates for the EU. Out of 75 countries measured, Romania was tied for first (with Ukraine, another postcommunist country) with a “perfect” score of 7; In a finding consistent with the varieties of capitalism argument, while the study calls labor flexibility one of twenty “engines of growth” it concedes that regression analysis finds no correlation between flexibility and growth (Warner, 2002).

¹³ Data are missing for Estonia and Slovakia, and Bulgaria's figures are from 2000 (Vaughan-Whitehead, 2003, p. 53).

Slovakia.¹⁴ Labor force participation rates, while rising in core EU member states, are declining in the new member states, the opposite of the hoped-for convergence (Vaughan-Whitehead, 2003; Riboud, Sanchez-Paramo, and Silva-Jauregui, 2002). More troubling still, a higher proportion of those unemployed in the region are long-term unemployed, with the long-term unemployment rate (those unemployed more than one year) 7.1% in the ten prospective members in 2001, as opposed to only 3.3% in the EU (Vaughan-Whitehead, 2003).

Some studies have blamed rigid labor markets and generous unemployment benefits for high-levels of unemployment in western Europe, in contrast to the more flexible labor markets, less generous unemployment benefits, and lower levels of unemployment found in liberal economies, especially the U.S. (OECD, 1994). Yet regarding labor markets in east central Europe, as we have seen there is little evidence that labor market rigidity might explain the region's such persistently high unemployment rates. Regarding unemployment benefits, those working in the varieties of capitalism perspective have found that high levels of unemployment (and employment) protection are an essential complement to the high-skills training and production profile of coordinated economies, since such benefits allow firms to attract and retain workers with high or specific skills (Estevez-Abe, Iversen, and Soskice, 2001). Following this, since the countries of east central Europe have not sought to create a coordinated system of skills training, we would expect there to be less institutional support for the maintenance of unemployment benefits. Not surprisingly then, the level of unemployment has remained steady in the region despite tougher eligibility requirements and reduced overall funding, so much so that in several countries, nearly half of those eligible don't bother to register for unemployment benefits (Vaughan-Whitehead, 2003, p. 197).

Moreover, a World Bank study from 2002 found that while the ratio of wages to unemployment benefits in east central Europe was not considerably lower than that found in OECD countries, spending on both active and passive labor market policies was substantially lower than the averages in the EU or the OECD. Looking at spending

¹⁴ Unemployment has remained particularly high in Poland and Slovakia where unemployment rates in December 2004 reached 18.3% and 16.9% respectively, and where the economies have otherwise appeared relatively strong (Euro-Stat, 2005).

relative to the number of unemployed, government spending on passive policies was 0.06 in the future member states, compared with an average of 0.26 for existing EU members and 0.23 for OECD members. (The U.S. figure was also 0.06, the lowest of any OECD member). Likewise, for active policies, the average for future members was 0.04, as opposed to .16 for existing EU members and 0.14 for the OECD. (The 0.04 figure is again identical to that of the U.S., second lowest in the OECD after Japan [0.02].) (Riboud, Sanchez-Paramo, and Silva-Jauregui, 2002).

Tax policy provides another, and rather striking, example of the liberal direction of the postcommunist member states. Here one finds low tax rates on capital, and a substantial shift in tax burdens from capital to labor and consumers (Appel, 2005). Moreover, and in what will most likely contribute to greater inequality, a number of countries in the region have introduced a flat income tax. Starting with the three Baltic countries in 1994-5, where the rates ranged from 33-25%, Slovakia adopted a flat tax rate of 19% in 2004 and Romania adopted a flat rate of 16% in 2005.¹⁵ Such tax policies almost certainly reflects the weakness of labor in these societies. More importantly for our current discussion, such policies are consistent with attempts to attract foreign capital through the liberal road of relatively low wages, flexible labor markets, and low tax burdens on capital (Bohle and Greskovits, 2005). Needless to say, this stands in stark contrast to the coordinated model.

To summarize the many different measures of varieties of capitalism we have looked at, the new EU member states of east central Europe appear to be firmly in the liberal camp. Slovenia is a clear exception, and appears to be firmly in the coordinated category.¹⁶ To put it starkly, in terms of the varieties of capitalism and labor relations of the new member states, the score is liberal 9, coordinated 1. The evidence presented here is in line with the conclusion of Bohle and Greskovits (2005, p. 40) that "empirical

¹⁵ In what would appear to be a case of the proverbial "race to the bottom," Estonia, the first postcommunist country to introduce the flat tax in 1994, is now planning on lowering its rate from 26% to 20% by 2007. "The Case for Flat Taxes," *The Economist*, April 14, 2005.

¹⁶ While based on some of the quantitative data we have presented, Slovakia may appear to be a second possible exception, overall Slovakia has fairly clearly chosen the liberal route to attracting capital and achieving international competitiveness (Malova and Haughton, 2005; Malova, 2005; Bohle and Greskovits, 2005).

evidence suggests that instead of convergence, rather divergent social standards have emerged."¹⁷

Slovenian Exceptionalism

How might we explain why Slovenia appears to be so different from other postcommunist states? On the one hand, one might be tempted to dismiss Slovenia as a relatively small country with little additional significance. Yet the differences between it and the other postcommunist countries are striking. At the very least – and this is one of the main points of the varieties of capitalism argument – the example of Slovenia would suggest there is indeed an alternative to an international competitiveness strategy based on flexible labor markets and low labor and social standards as a means of attracting foreign capital.

Indeed, Slovenia not only fares well compared to other postcommunist countries in terms of labor standards, but also in terms of economic indicators – it is by most measures the most successful of postcommunist economies. Its standard of living and wages are the highest of the new member states, and already approach EU standards. Certainly this is a model to be emulated.

However, the Slovenian experience also underscores another tenet of the varieties of capitalism argument – that coordinated market economies are the products of specific historical circumstances, and are very difficult to bring about. While a full explanation of the Slovenian deviation lies beyond the scope of this paper, a few general points can be made, most pointing to the advantages of Slovenia's starting point, before the transition began. Slovenia's social system appears to be modeled most closely on Austria, to whom it is close geographically and also historically as a former subject of the Hapsburg empire (Lado, 2002). However, this history and geography would not make it unique within east central Europe. More importantly, Slovenia was a republic within Yugoslavia, and this had several consequences. Yugoslavia was the most market-oriented of countries within

¹⁷ We have not attempted to explain here why (with Slovenia the exception) eastern European countries have adopted liberal labor and social policies. Elsewhere it has been argued that postcommunist legacies created weak labor movements (Crowley, 2005) while others point to the impact of globalization (Kubicek, 2004) international financial institutions (Vaughan-Whitehead, 2003) and foreign direct investment (Bohle and Greskovits, 2005).

communist eastern Europe, and since it was outside the Soviet bloc, it had extensive relations, including trade relations, with the capitalist world. The Yugoslav socialist model was largely based on the idea of "self-management," which, while still dominated by the League of Communists, gave substantial leeway to workers within the enterprise. Unlike other eastern European countries (excepting Albania), communist rule came about in Yugoslavia through an indigenous revolution, and thus it and the self-management experiment appeared home-grown and therefore legitimate rather than one imposed by Soviet tanks.

Much of this Slovenia shared with other Yugoslav republics, so why did it perform so much better than them? Perhaps most importantly, Slovenia was the most 'western' of the Yugoslav republics, both in terms of geography, and also in terms of its market orientation, its trade profile, and its standard of living. It was also the most ethnically homogenous, and it was the first republic to seceded from the Yugoslav federation, arguing that it would do better alone, without having its surplus distributed to poorer Yugoslav republics. Also in significant contrast to other Yugoslav republics, it was able to achieve independence in days, with a minimal amount of bloodshed. Thus upon independence, Slovenia was a largely market-oriented economy already, with a higher standard of living than any other former communist country. As such, it was less susceptible to IMF pressure, and partly as a result, able to pursue a "gradualist" approach to economic transformation, and the initial recession was not as severe as elsewhere (Vaughan-Whitehead, 2003, pp. 128-9; Feldmann, 2006). Slovenia's profile as a small, relatively open European economy, as well as the existing institutions of self-management which were largely seen as legitimate by society, contributed greatly to its current coordinated labor and social welfare policies.

Again, as with the varieties of capitalism argument, the Slovenian case suggests that there is an alternative to liberal capitalism, but that this alternative is the result of complex historical factors rather than a menu of readily available policy choices. Yet that does not mean that countries like Slovenia are impervious to international pressures. Despite its successes, the World Bank has placed pressure on Slovenia bank to reduce social expenditures (Vaughan-Whitehead, 2003). Less predictably, the ILO is pushing

Slovenia to change its collective bargaining system, to make it "voluntary" rather than "compulsory" (Feldmann, 2006).¹⁸

European harmonization and the varieties of capitalism

What are the consequences of the finding that nine out of ten new member states are much closer to liberal rather than coordinated market economies? Let us consider three sorts of questions: the likelihood of harmonizing the labor and social policies of new members "upwards" toward existing European levels, the potential implications for varieties of capitalism theoretical perspective, and the potential impact of eastern liberalization on the coordinated economies of western Europe.

Regarding harmonization, one might argue that, even if all the above weaknesses in east European labor relations are true, convergence to pre-accession European standards is still possible, perhaps even likely. The southern European countries, one might point out, especially Portugal, Spain and Greece, are often closer to the countries of east central Europe in terms of labor market institutions than other EU members. Not accidentally, one might add, these countries were also among the last to join the EU, and they are also below the EU average in terms of economic development, but in this regard have converged toward the mean over time. Moreover, if comparisons were made to non-European countries with similar levels of economic development, such less developed countries would likely look more similar to eastern European countries in terms of labor institutions and social policies. To the extent that in the communist period these societies displayed certain surface similarities with the European social model, it was because they were, in Kornai's phrase, "premature welfare states" (1992). On the other hand, the argument might run, the Slovenian case, with the highest standard of living of the new member states, points to their future – as their standards of living increase, they will then be able to develop similar labor and social institutions.

There are, however, some strong reasons to doubt the ultimate validity of such an argument. Consider first the likelihood that east central European countries will follow

¹⁸ Interestingly, almost uniquely among European countries, the main Slovenian trade union has joined critics in calling for greater decentralization of collective bargaining to the sectoral level, while the employers are pushing to retain the system of centralized bargaining (Schulten, 2005).

the economic trajectory of Portugal, Spain and Greece. The new member states of eastern Europe are considerably less well-off than the southern European countries were when they joined the Union, and they also have larger gaps with the EU in wages and social standards. The "structural funds" that were distributed from wealthier EU members to the southern European countries will apparently be less generous for the new member states, in part because there are more of them and their total population is greater. Even with these advantages, Portugal, Greece and Spain have only been slowly catching-up in terms of workers' earnings, with Portugal and Greece still only 40% and 50% of the EU average in real earnings per employee (Vaughan-Whitehead, 2003, pp. 336-7). In terms of convergence in standards of living, most scenarios suggest it will take 20-30 years for the new members to reach EU averages, and even then only on the assumption that the growth of new members consistently outstrips that of west European economies.

However, even if the hoped-for economic convergence were to take place, there are strong reasons for doubting that the labor and social standards of east central Europe societies would "catch up" as well. Most importantly, such a prediction runs directly counter to the central insight of the varieties of capitalism argument – that a number of wealthy capitalist societies are liberal, and that convergence across varieties of capitalism rarely occurs.

The reasons for doubting that social harmonization will occur become clearer if we turn to the institutional theories on which much of the varieties of capitalism argument is based. The same reasons that the proponents of the varieties of capitalism view are "optimistic" about the resilience of the coordinated market economies suggest that one should be "pessimistic" about the prospects for further dramatic change (in a different direction) in east central Europe. The institutional theory upon which the varieties of capitalism argument rests emphasizes notions of path dependence, increasing returns and lock-in effects, all of which suggest institutional arrangements, once established, are very difficult to change. Institutional arrangements do of course change, but dramatic changes, such as the development of dramatically different labor and social institutions, are said to occur only when an exogenous shock or critical juncture creates a moment of institutional openness.

Of course, no part of the world has experienced more dramatic institutional change in recent years than postcommunist eastern Europe, but this merely increases the doubts about further significant change. For to call the collapse of communism a "critical juncture" grossly understates the nature of the postcommunist transformations, which are perhaps better captured by theories of revolutionary change in terms of their scope. Among other changes, postcommunism entailed the transfer of entire economies from the state to private hands, establishing a class of previously non-existent property owners in the process. While this is institutional change of historic proportions, this transformative period, or moment of institutional openness, has now come to a close. In this sense, the postcommunist era has ended, although as institutional (and revolutionary) theory suggests, the ways in which postcommunism was resolved will have long-lasting consequences. While critics have pointed out correctly that such "punctuated equilibrium" models do not explain all forms of institutional change, the postcommunist period would appear to be an exemplary case of punctuated equilibrium.

And yet while the varieties of capitalism perspective, as this paper has argued, can provide considerable insights into the political economies of the new EU member states, the postcommunist experience raises at least three difficult questions for this theoretical approach. First, why did nine out of ten postcommunist countries end up with liberal rather than coordinated labor institutions, and what does this say about the varieties of capitalism? Second, even if the result of an "exogenous shock," what does the rapid and fundamental transformation of institutions in these countries say about the perspective's assumptions about institutional resilience? And third, how realistic is the expectation that coordinated economies in Europe will continue to be resilient when faced with, along with existing pressures, ten new members of the European Union with economies organized along liberal lines? Let us consider these questions in turn.

While a full explanation of why postcommunist societies of east central Europe adopted liberal institutions would require a separate paper, one could point to a number of factors, especially various international pressures placed on small, relatively poor countries seeking to attract foreign capital, as well as certain legacies of the communist period that both helped weaken labor movements and prompted a number of these societies to embrace radical change. But it also appears difficult to imagine how

coordinated institutions might have evolved in most of these countries. If, in coordinated markets, coordination is carried out by private actors seeking to advance their interests in a market environment, in postcommunist societies those private actors as organized interests were weak and in some cases nearly non-existent. The incentives for coordination between these actors were lacking, and it is difficult to see from where these incentives might have arisen, especially in societies where foreign rather than domestic capital is dominant. Indeed, the near-absence of coordination among postcommunist cases underscores what others have argued from examinations of the development of coordinated institutions elsewhere -- that the development of coordinated market economies appears to be particularly historically contingent (in some cases based on traditions going back to the 19th century) and difficult to construct (Streeck and Yamamura, 2001; Howell, 2003). Taken together, this evidence suggests that there is a considerable unevenness to the varieties of capitalism: while varieties exist, some varieties are harder to create, and arguably harder to maintain, than others (Streeck and Thelen, 2005).

Moreover, we should note that the liberal model that these countries adopted ran counter to many of the existing institutions of the communist period, such as high levels of union membership and collective bargaining, and a certain amount of coordination entailed in the planning mechanism. To be sure, such institutions bore only a surface resemblance to those of a coordinated market economy. However, whereas the varieties of capitalism approach argues that a society's institutions will shape its competitiveness strategy, in the postcommunist cases the causal arrow appears to have been reversed. Indeed, to the extent that the new member states could be said to have chosen a strategy, it has been the liberal road to achieving comparative advantage: appealing to (primarily foreign) capital on the basis of relatively low wage costs and limited regulations as opposed to high-skills and value-added production. As recent changes in tax policy suggest, in path dependent fashion, regardless of why they the liberal path was initially adopted, later policy choices tend to reinforce that inclination.

What impact could the ten new liberal member states have on the continued viability of the coordinated market economies of Europe? Much of the literature on accession has demonstrated how EU mandates constrained the relatively weaker

applicant countries; one could argue, however, that regarding labor and social policies, the poorer and weaker countries of east central Europe will likely impact the wealthier, more established EU members more than the other way around.

This is arguably so because the varieties of capitalism perspective has likely overstated the resilience of the coordinated model against global pressures for liberalization. As Streeck and Thelen (2005) have argued, the punctuated equilibrium model of institutional change on which the varieties argument rests misses how liberalization pressures can lead to change that is both incremental and transformative. Moreover, the model of coordinated markets draws heavily on the experience of Germany, where there is growing evidence of the weakening of coordination in industrial relations, not least because of the integration of the former communist East Germany (Howell, 2003). German politicians continually speak of the pressures for further liberalizing reform; it is hard to imagine what sort of pressures eastern European governments might invoke to justify reform in a more coordinated direction. Rather, the new member states, in areas such as union density, collective bargaining coverage, levels of inequality and tax policy, are clearly swimming with the tides of liberalizing trends. Thus, as Meardi (2000; 2002) has argued, rather than being "behind" western Europe in the development of market institutions, postcommunist eastern Europe might be the vanguard of further liberalization.

Further, the pressures on the liberalization of coordinated economies might increase because of consequences of EU expansion that we have hardly mentioned – the ability of west European capital to move production facilities next door to countries that now enjoy the benefits of being inside the EU, but where skilled labor is not only a fraction of the cost, but is also much more flexible than in the old member states. It is through this process that fears of "social dumping" are generated, as well as the reciprocal and more widely expressed fear that labor will migrate in the opposite direction, further undercutting labor markets in western Europe. In short, while EU expansion is by no means the only source of pressure for liberalization in western Europe, it is a significant additional pressure, and among scholars if not the general public, it is to date a significantly underestimated one.

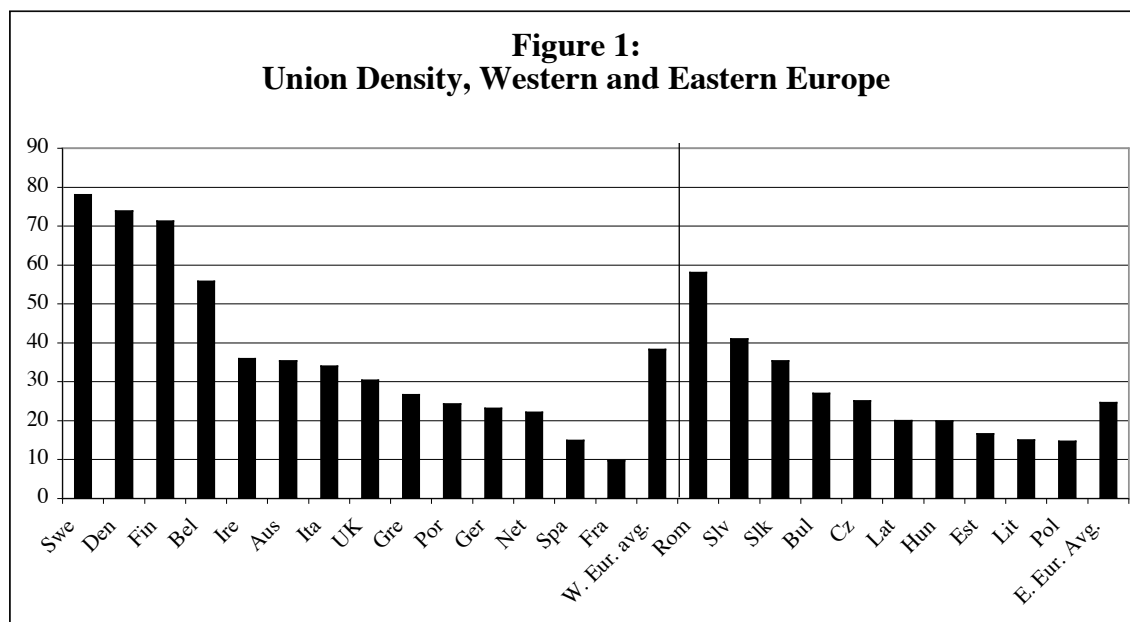
Politically, concerns about eastern labor markets, in the guise of the "Polish plumber," have already played a central role in derailing the EU constitution. Moreover, the inability of the EU expansion process to include labor and social concerns in a meaningful way has arguably exposed the weakness of existing EU social legislation, as well as the pretension that the EU is nurturing a distinct "European social model" rather than merely economic integration.

We have argued that the varieties of capitalism argument provides valuable insights into understanding the new postcommunist EU members, and that following the dichotomy used in the varieties of capitalism literature, the new member states, with the exception of Slovenia, are clearly more "liberal" than "coordinated." When applied to east central Europe, the varieties of capitalism approach, particularly its perspective on institutional change, leads to skepticism that these countries will converge or harmonize toward EU norms regarding labor and social policies. However, while this paper has relied on the theoretical insights of varieties of capitalism perspective, it has done so in a way that undercuts the normative thrust at the center of that theoretical approach – namely that the coordinated market economies will continue to resist convergence toward the global trend of liberalization. The new member states of eastern Europe won't bring about this liberalization by themselves, but they are already providing a significant additional impetus.

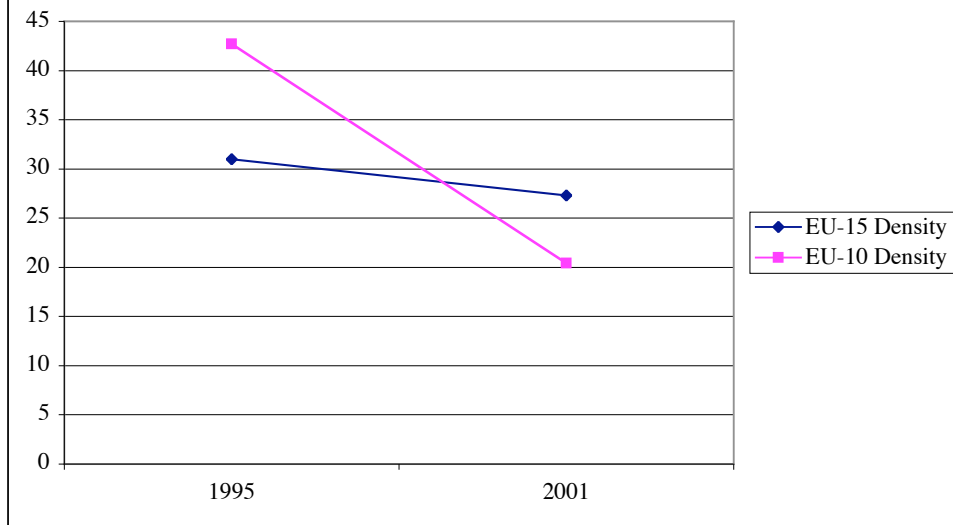
Table 1
Coordinated versus liberal market economies
(industrial relations)

	coordinated market economies	liberal market economies
union density	high	low
dominant level of collective bargaining	national or sectoral	firm
rates of collective bargaining coverage	high	low
social dialogue	strong	weak to non-existent
employers' organization	strong	weak to non-existent
vocational training	employer cooperation/ specific skills	formal education/ general skills
workers' participation in firm	significant	weak to non-existent

sources: adapted from Feldmann; Hall and Soskice.



**Figure 2:
Trends in Density Rates, Old and New EU
Members**



**Figure 3:
Collective Bargaining Coverage Rates,
Old and New Europe**

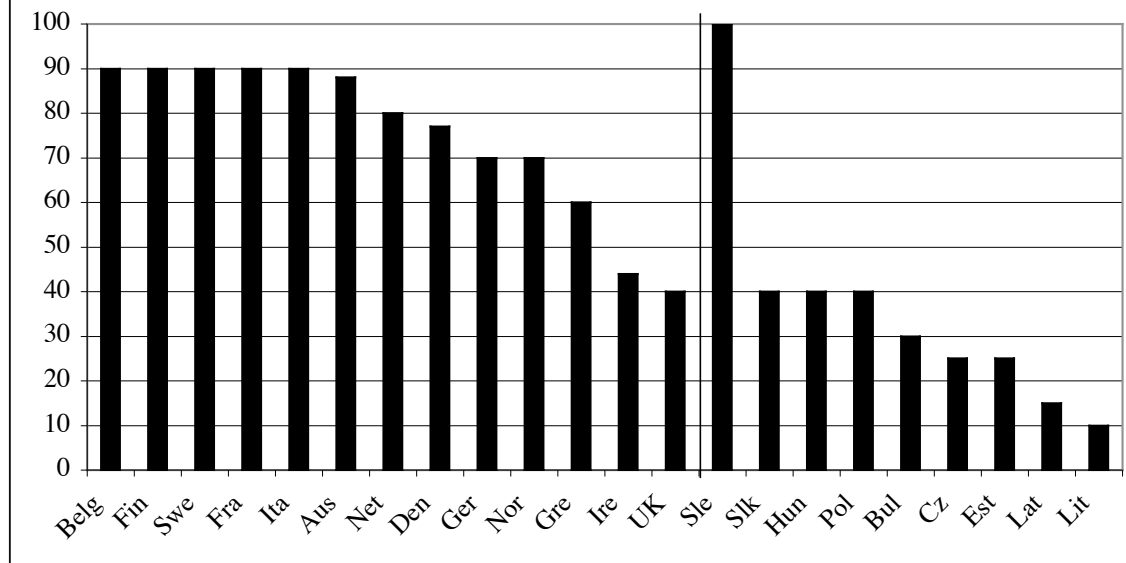


Table 2:
Dominant Level of Collective Bargaining

	Intersectoral	Sectoral	Company
Belgium	XX		
Finland	XX		
Ireland	XX		
Austria		XX	
Denmark		XX	
Germany		XX	
Greece		XX	
Italy		XX	
Netherlands		XX	
Norway		XX	
Spain		XX	
Sweden		XX	
France	(no dominant level)		
UK			XX
Slovenia	XX		
Slovakia		XX	
Bulgaria		XX	
Czech R.			XX
Estonia			XX
Hungary			XX
Latvia			XX
Lithuania			XX
Poland			XX
Romania			XX

Figure 4:
Centralization of Wage Bargaining Index

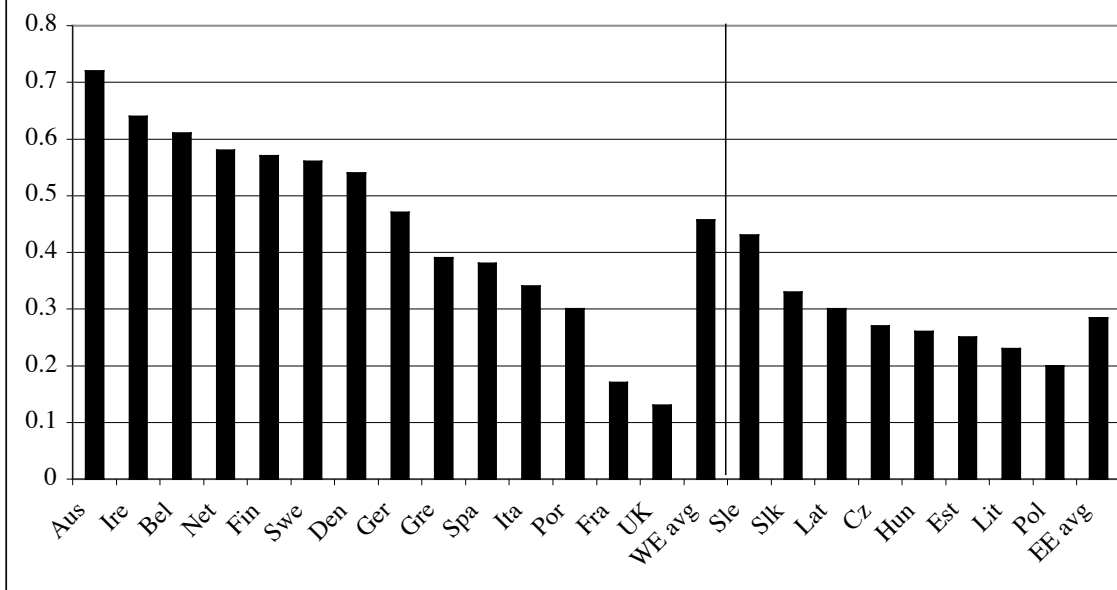
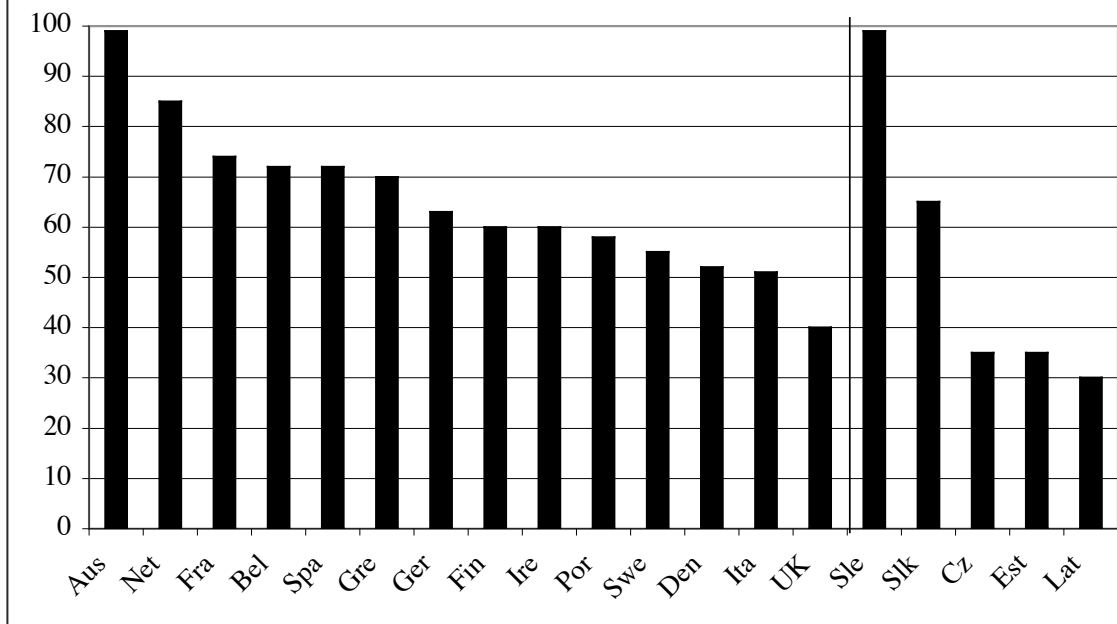


Figure 5:
Employers' Associations, Organization Rate



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