

COMMENT

ON THE ECONOMIC REALITIES OF THE EUROPEAN SOCIAL CHARTER AND THE SOCIAL DIMENSION OF EC 1992

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I. INTRODUCTION

In late 1989, the heads of state of the nations comprising the European Community (EC) adopted the Community Charter of Fundamental Social Rights¹ which sets forth the broad parameters of the social dimension envisioned as part of the coming economic unification of Europe (EC 1992). The Social Charter states that a critical part of the forthcoming economic unification of the EC is the promotion of "improved living and working conditions for workers."² To this end, the Social Charter establishes broad goals in terms of greater freedom of movement, standardization of protection, and increased equality for all workers throughout the EC.³

More recently, the European Commission began to effectuate some of the broad goals of the Social Charter through an Action Programme⁴ and various specific directives.⁵ It states that one of its primary goals is

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1. Community Charter of Fundamental Social Rights, COM(89)471 final [hereinafter Social Charter].

2. *Id.* pmb1.

3. *Id.* §§ 1-3, 15, 19, 24-26.

4. Communication from the Commission Concerning Its Action Programme Relating to the Implementation of the Community Charter of Basic Social Rights for Workers, COM(89)568 [hereinafter Action Programme].

5. Proposal for a Council Directive on Certain Employment Relationships with Regard to Working Conditions, 1990 O.J. (C 224) 4; Proposal for a Council Directive on Certain Employment Relationships with Regard to Distortions of Competition, 1990 O.J. (C 224) 5; Proposal for a Council Directive Supplementing the Measures to Encourage Improvements in the Safety and Health at Work of Temporary Workers, 1990 O.J. (C 224) 6.

the reduction of unemployment, particularly long-term unemployment.⁶ The Action Programme also calls for increased social dialogue throughout the EC, including broad worker involvement and consultation with respect to major business decisions and increased participation in financial matters for the purpose of promoting "greater justice in the distribution of wealth."⁷

In late 1990, the Commission issued its first group of significant proposed directives pursuant to the Action Programme.⁸ The proposals deal with the topic of atypical (part-time and temporary) work.⁹ The thrust of these proposed directives is to afford part-time and temporary workers, at least on a pro rata basis, the same training, insurance, vacation, seniority, and other benefits as full-time employees.¹⁰

While the overall goals of the Social Charter and the Action Programme, to improve worker "living and working conditions"¹¹ and to reduce unemployment, are quite laudatory, this Commentary will argue that the approach being taken by the European Commission may not achieve these goals. Indeed, it will be averred that in many respects the aforementioned documents are quite protectionist in nature, and are likely to protect the citizens of the wealthier EC nations.¹² This Commentary will further argue that this protectionist approach may ultimately reduce the volume of free trade among the twelve member states of the EC, and among the nineteen member countries of the newly formed European Economic Area.¹³

Economic growth is the most certain cure for long-term unemployment throughout the European Community. The implementation of the Action Programme will reduce opportunities for growth in the EC by reducing the differences among labor markets in EC countries. This policy may protect some jobs in the short-run, but it will limit the opportunities for countries to trade on the basis of their individual comparative advan-

6. Action Programme, *supra* note 4, at 5-6.

7. *Id.* at 33.

8. See *supra* note 5.

9. See Peter S. Pantaleo & Leonard Bierman, *Proposed Directives on Part-time Work—A Potential Full-time Burden?*, 2 J. EUR. BUS. 49 (1990). For the British reaction to these proposals, see also Employment Department (U.K.), *European Commission Goes Ahead with "Unnecessary and Misguided" Directives on Part-Time and Temporary Employment* (Press Notice 221/90, June 13, 1990).

10. Pantaleo & Bierman, *supra* note 9, at 51-52.

11. Social Charter, *supra* note 1, at 1; Action Programme, *supra* note 4, at 6.

12. See Victoria Curzon Price, *The Threat of "Fortress Europe" from the Development of Social and Industrial Policies at a European Level* (1990) (unpublished manuscript, on file with the Texas A&M Business School).

13. See Mark Maremont & Richard A. Melcher, *Tearing Down Even More Fences in Europe*, *Bus. Wk.*, Nov. 4, 1991, at 50, 50-52; Alan Riding, *Europeans in Accord to Create Vastly Expanded Trading Block*, *N.Y. TIMES*, Oct. 23, 1991, at A1. The European Economic Area is comprised of the EC member states plus Sweden, Austria, Finland, Switzerland, Norway, Iceland, and Liechtenstein.

tage.¹⁴ Such trade increases the wealth of all trading partners and provides the stimulus for continued economic growth; more growth means more jobs. Thus, despite the laudatory language, the ultimate effects of the proposals on the social dimension of the European Community may be quite pernicious in nature.

II. SOCIAL DUMPING

The drive toward economic unification of the EC and the recent establishment of the European Economic Area are, in part, responses to the development of other trading blocs in the world, such as the economic unification of the United States and Canada in 1989 through the Canada-United States Free Trade Agreement¹⁵ and the impending joinder of Mexico into that Agreement.¹⁶ If Europe is to compete effectively against larger trading blocs there has to be free trade and greater economic cohesion within the EC and the European Economic Area. Thus, the overall thrust of EC 1992 and of the new European Economic Area is to deregulate and relax the barriers to exchange.¹⁷ The proposed development of a European currency is, for example, one clear illustration of an attempt to ease trade barriers.¹⁸

With freer European exchange and trade comes, however, a fundamental fear felt by the wealthier northern European countries. The fear is one of social dumping. If it will be just as easy to conduct business from Spain and Portugal as it is from Germany, there will be clear incentives for new businesses to open in those countries where wages are low and workers' demands for improved working conditions are not as far reaching.¹⁹ The purported concern is that under such a construction the wealthier countries will then be forced to lower their working standards in

14. Comparative advantage may be defined in the following manner: "In a world of competitive markets, trade will occur and be beneficial whenever there are international differences in relative costs of production." PETER B. KENEN, *THE INTERNATIONAL ECONOMY* 14 (2d ed. 1989).

15. See generally Leonard Bierman & Donald R. Fraser, *The Canada-United States Free Trade Agreement and U.S. Banking: Implications for Policy Reform*, 29 VA. J. INT'L L. 1 (1988).

16. See generally Review Of Trade And Investment Liberalization Measures By Mexico And Prospects For Future United States-Mexican Relations, USITC Pub. 2275, Inv. No. 332-282 (April 1990). But see Henry F. Myers, *The Outlook: Talk of Trading Blocs May Exaggerate Risks*, WALL ST. J., Oct. 21, 1991, at A1.

17. See, e.g., AUDREY WINTER ET AL., *EUROPE WITHOUT FRONTIERS: A LAWYER'S GUIDE* (BNA Corporate Practice Series 1989); Riding, *supra* note 13.

18. See Nigel M. Healey, *Whither European Monetary Union?*, 256 CONTEMP. REV. 128, 128 (1990). See Alan Riding, *Europeans Agree on a Pact Forging New Political Ties and Integrating Economies*, N.Y. TIMES, Dec. 11, 1991, at A1, for a report of the reaching of a new agreement. It should be noted that Britain opted out of the monetary union as well as provisions on social policies. *Id.*

19. See Johnathan Kapstein et al., *Workers Want Their Piece of Europe Inc.*, BUS. WK., Oct. 29, 1990, at 46, 46. See generally Stephen J. Silvia, *The Social Charter of the European Community: A Defeat for European Labor*, 44 INDUS. & LAB. REL. REV. 626, 633 (1991).

order to compete effectively with such economic movement, and that will lead, as some observers have stated, to the "Portugalization of Europe."²⁰

The solution to this dilemma devised by Germany and other wealthy EC countries, as set forth in broad-brush form in the Social Charter and Action Programme, is to impose uniformly high standards of worker protection throughout the EC.²¹ For example, Germany has, pursuant to its Co-determination and Labor Management Relations Acts,²² an extremely comprehensive system of worker participation at both the corporate board of directors and plant levels.²³ In contrast, various other EC countries, such as Italy and Ireland, currently have no formal worker participation requirements, while most others have significantly less stringent requirements than those in Germany.²⁴ The European Commission Action Programme, however, calls for the "[e]stablishment of equivalent systems of worker representation in all European-scale enterprises . . ." including "equity-sharing and financial participation by workers."²⁵ Similarly, while workers in Denmark and France currently receive six weeks of vacation a year, employees in many other EC nations receive considerably less time off.²⁶ Various European Commission proposals would increase worker time off on an across-the-board basis throughout the EC.²⁷

While this approach of imposing higher uniform worker protection standards may suit countries like Denmark and Germany, it represents, as will be developed below, bad economics from the perspective of European consumers and most European workers. It may also ultimately jeopardize the efficacy of a unified common market and the operation of the European Economic Area.

III. COMPARATIVE ADVANTAGE AND THE BASIS OF TRADE

The underlying difficulty with the purported solution to the social dumping problem is that it overlooks a fundamental economic reality: trade is based on differences.²⁸ By overlooking this basic principle, the

20. See Kapstein et al., *supra* note 19, at 46. See also *Europe's Social Insecurity*, THE ECONOMIST, June 23, 1990, at 13.

21. See generally Silvia, *supra* note 19, at 633-34.

22. Mitbestimmungsgesetz [MitbestG], 1976 Bundesgesetzblatt [BGBl] I 1153 (F.R.G.); Betriebsverfassungsgesetz [BetrVG], 1972 BGBl I 13 (F.R.G.).

23. See generally Michael Gruson & Wienand Meilicke, *The New Co-Determination Law In Germany*, 32 BUS. LAW. 571 (1977); Michael Kaplan, Comment, *Is Labor a Widget: A Comparative Study*, 59 TUL. L. REV. 1517, 1540-47 (1985).

24. See Rae Sedel, *Europe 1992: HR Implications of the European Unification*, PERSONNEL, Oct. 1989, at 19, 22.

25. See Action Programme, *supra* note 4, at 33.

26. See Sedel, *supra* note 24, at 22.

27. See generally Pantaleo & Bierman, *supra* note 9, at 50.

28. See generally KENEN, *supra* note 14, at 13-50.

framers of the Social Charter ignore the concept of comparative advantage which is an important attraction for businesses when choosing to set up their operations in poorer countries. As one British executive recently stated, "if you force Spain and Portugal to get to the level of Germany" you will have considerable reason "not to go there."²⁹ Although some countries may be very good at producing many things, every country will have a comparative advantage at manufacturing specific items or providing certain services. It is important to understand, however, that the concept of comparative advantage is not the same as absolute advantage.

For example, suppose a young attorney is beginning a new practice and she decides to hire a secretary primarily for word processing. After advertising the position and interviewing a number of respondents in the local labor market, the attorney finds that the best candidates can do word processing at a rate that is a little slower than the attorney. That is, the attorney has an absolute advantage at word processing compared to all the available job candidates.³⁰ Every hour the attorney spends doing word processing, though, is an hour that could be spent doing legal work which could be billed at approximately \$200 per hour. Of all the candidates interviewed for the secretarial job, the best ones may have alternative opportunities to earn, perhaps, \$15 per hour. Thus, the opportunity cost for the secretary to produce an hour of word processing is far less than the opportunity cost for the attorney, even though the attorney is faster at the keyboard. The secretary has a comparative advantage at producing word processing relative to the attorney. If the attorney hires one of the good secretarial candidates both will be better off. The attorney will be able to spend more of her time doing billable legal work and the secretary will be able to earn a higher salary than may be available to him in the general job market.³¹

Countries with cheap labor have a large supply of workers who have few present opportunities to work for higher wages. Such countries thus have a comparative advantage in terms of the production of certain types of goods. The chart below (Chart 1), outlining hourly manufacturing wages in various European countries, helps illustrate this point:

29. Kapstein et al., *supra* note 19, at 46.

30. See JAMES D. GWARTNEY & RICHARD L. STROUP, *MICROECONOMICS: PUBLIC AND PRIVATE CHOICE* 43 (5th ed. 1990) (using a similar example to illustrate comparative and absolute advantages).

31. *Id.*

CHART 1³²
 Gross Hourly Wages in the Manufacturing Industry
 (in U.S. Dollars)

	1970	1980	1989
West Germany	\$1.70	\$7.36	\$10.25
France	\$1.07	\$5.26	\$6.84
Italy	\$1.01	\$4.64	\$7.60
Great Britain	\$1.32	\$5.61	\$8.97
Denmark	\$2.03	\$9.33	\$12.44
Netherlands	\$1.33	\$7.21	\$8.63
Spain	\$0.57	\$4.03	\$6.70
Portugal	n/a	\$1.46	\$2.00
Greece	\$0.54	\$2.36	\$3.38
Ireland	\$1.02	\$5.10	\$7.22
United States	\$3.36	\$7.25	\$10.47
Japan	\$0.94	\$5.41	\$12.18

The wide disparity in average hourly manufacturing wages across the EC is obvious from the chart. At the present time, latest available figures show wages ranging from highs of \$12.44³³ and \$10.25 per hour in Denmark and Germany to lows of \$3.38 and \$2.00 per hour in Greece and Portugal. Changes in wages are usually associated with changes in the productivity of labor.³⁴ Moreover, wages are not necessarily static. In some countries, wages dramatically jumped between given time periods while in other countries they remained more or less the same.

It is critical to note that at the current time countries like Portugal and Greece have a clear comparative advantage in terms of low-cost manufacturing labor. The Portuguese hourly manufacturing wage is, for example, only about sixteen percent of the Danish hourly wage and twenty percent of the German wage. Thus, a company seeking low-skilled labor can, for a given dollar, purchase five or six times more labor in Portugal than it can in Denmark or Germany.

There are clear incentives for companies in need of low-skilled or unskilled labor to open operations in Portugal and other relatively low labor-cost countries, as they have done in considerable numbers over the

32. INSTITUT DER DEUTSCHEN WIRTSCHAFT KÖLN, INTERNATIONAL ECONOMIC INDICATORS 55 (1991).

33. All references to monetary units will be in terms of United States currency.

34. See Edward Balls, *European Unit Labour Costs Converge*, FIN. TIMES, Nov. 11, 1991, at 1. See also GWARTNEY & STROUP, *supra* note 30, at 326-27.

past few years.³⁵ Even companies that prefer the social and other amenities of a country like Denmark will be encouraged by market phenomena to consider shifting low-skill operations to places like Portugal and Greece. In turn, however, if Brussels raised Portuguese and Greek hourly wages to the same level as those in Denmark and Germany, then, as the aforementioned British executive pointed out, the incentive to open operations in those countries would be reduced.³⁶ Portuguese and Greek labor is simply not yet productive enough to merit the \$10 plus per hour wages earned in Denmark and Germany. Moreover, Portugal and Greece may not, at the present time, be endowed with national infrastructures that will allow their average manufacturing workers to earn these kinds of wages.³⁷ In short, a scheme mandating the equalization of wages among these countries would hinder the economic development in countries like Portugal and Greece because their key comparative advantage, low-cost wages, would be eliminated. At the same time, countries like Denmark and Germany would be helped by such a scheme since it would remove a major incentive for businesses to set up shop elsewhere, and reinforce any absolute advantages that these countries already enjoy.

IV. TOTAL LABOR COSTS ARE MORE THAN HOURLY WAGES

It is, of course, almost impossible that Brussels will mandate that all workers in the EC be paid the same exact hourly wages, although a minimum wage has been suggested.³⁸ It is important to keep in mind that total labor costs are more than just hourly wages. Labor costs also include various fringe benefits normally provided to workers, such as retirement contributions, health insurance, and so forth. These fringe benefits, as the chart below illustrates (Chart 2), vary considerably across countries.

35. See generally Kapstein et al., *supra* note 19, at 46.

36. See *supra* note 29 and accompanying text.

37. See generally WORLD ECONOMIC FORUM, *THE WORLD COMPETITIVENESS REPORT 1991*, 59, 89 (1991). See also GWARTNEY & STROUP, *supra* note 30, at 552-53, for a discussion of various factors, including national infrastructure, which affect economic growth.

38. See Kapstein et al., *supra* note 19, at 46.

CHART 2³⁹
*Hourly Earnings Plus Fringe Benefits in the
 Manufacturing Industry
 (in U.S. Dollars)*

	1970	1980	1989
West Germany	\$2.58	\$12.89	\$19.00
France	\$1.77	\$9.56	\$12.78
Italy	\$1.90	\$9.64	\$15.27
Great Britain	\$1.61	\$7.32	\$12.83
Denmark	\$2.40	\$11.50	\$15.31
Netherlands	\$2.19	\$12.79	\$15.44
Spain	\$0.84	\$6.43	\$10.89
Portugal	n/a	n/a	\$3.44
Greece	\$0.75	\$3.66	\$5.55
Ireland	\$1.22	\$6.68	\$10.37
United States	\$4.33	\$10.04	\$14.40
Japan	\$1.08	\$6.80	\$15.78

A careful examination of Charts 1 and 2 shows that in some countries, such as Italy, fringe benefits per hour are actually greater than wages, while in other countries, such as Denmark, fringe benefits represent a considerably lower proportion of the total wage package.⁴⁰ In contrast, Germany's total labor costs, wages plus fringe benefits, comes to \$19 per hour, which is considerably higher than any of the other listed countries, even though in terms of raw wages paid to workers its compensation scheme ranks below Denmark, the United States, and Japan. Yet, with fringe benefit costs added in, labor costs in Greece and Portugal are still very far below those in other countries, amounting to \$5.55 and \$3.44 respectively.

As noted above, while it is highly unlikely that as part of EC 1992 wages are going to be equalized across Europe by fiat,⁴¹ it is a goal of the Social Charter to increase fringe benefits throughout the EC.⁴² For example, the recent proposals made by the EC regarding atypical work mandate, among other things, that part-time and temporary workers receive various insurance and training benefits.⁴³

39. INSTITUT DER DEUTSCHEN WIRTSCHAFT KÖLN, *supra* note 32, at 56.

40. See *supra* notes 32, 39 and accompanying charts.

41. See *supra* note 38 and accompanying text.

42. See Social Charter, *supra* note 1, pmb.

43. See *supra* note 5.

Further, let us hypothesize that, on average, these new benefits requirements raise total labor costs by \$1 per hour. While an across-the-board \$1 per hour increase in labor costs seems fair, Chart 2 shows that the impact of such an increase will be extremely disproportionate. In Germany, a \$1 increase in fringe benefits will raise total labor costs by approximately five percent, while in Portugal such an increase will raise total labor costs by about thirty percent.⁴⁴ Such uniform increases in fringe benefits narrow the overall difference in total labor costs between highly developed countries like Denmark and Germany, and lesser developed countries such as Portugal and Greece. In short, mandated across-the-board increases in worker fringe benefits such as those contained in the atypical work proposals sharply reduce the comparative advantage that poorer EC countries have in terms of their overall labor costs.

Moreover, economists would also include requirements of worker consultation and participation in company decision making in the overall computation of labor costs.⁴⁵ In Germany, employers clearly view these requirements as costs, even with a work force which is highly educated and which may have much to contribute during such mandated participation in business decision making.⁴⁶ The proposed imposition of German-type worker participation on employers in countries like Portugal and Greece will thus levy the same, or, potentially, greater costs on these employers.⁴⁷ Such requirements further close the labor cost gap between these countries and the wealthier countries and thus reduce the basis for trade.

The EC Social Charter and the planned social dimension of EC 1992 envision greater equalization of labor costs throughout the EC by across-the-board increases in fringe benefits and worker participation rights.⁴⁸ But, as the above discussion points out, such increases in labor costs will not really promote greater equality among EC nations. They will, instead, ultimately advance greater inequality by reducing the comparative advantage of lesser developed European countries. The proposals, in the name of protecting against social dumping, will operate

44. German total wages are \$19, so a \$1 increase will represent a 5.26% boost of overall wages. In Portugal, however, total wages are only \$3.44, so a \$1 increase will represent a 29.4% jump in total wages. See *supra* note 39 and accompanying text.

45. See generally ARMEN A. ALCHIAN & WILLIAM R. ALLEN, EXCHANGE AND PRODUCTION: COMPETITION, COORDINATION AND CONTROL 393-94 (2d ed. 1977).

46. Under the present German codetermination law, companies with more than 2000 employees are required to put employees on their supervisory boards. MitbestG, 1976 BGBl. I 1153.

47. Portuguese and Greek workers are generally less well educated than workers in Germany and will most likely, on average, contribute less to boardroom and other strategic business decision making.

48. See *supra* notes 1-10 and accompanying text.

to protect countries like Germany and Denmark, at the expense of countries like Greece, Portugal, and Spain.

V. LOW WAGES NEED NOT BE PERMANENT

While some observers may see across-the-board increases in fringe and other worker benefits as helping workers in poorer countries by raising their standard of living,⁴⁹ such help will be of an extremely temporary nature. New employer requirements will raise the cost of doing business in these lesser developed countries relative to other EC countries, and eliminate the comparative advantage that they currently enjoy in terms of low wages. Indeed, the best way to increase low wages in these countries is to encourage trading based on each country's comparative advantage. As the economic developments in Japan over the past two decades illustrate, low wages need not be permanent, and are best overcome when trade increases the demand for goods which a country can produce when it has a comparative advantage.

In 1970, as Charts 1 and 2 point out, Japanese hourly wages were \$0.94 and wages plus formal fringe benefits were \$1.08. Approximately two decades later, Japanese wages are over \$12 per hour, and wages and fringe benefits are approximately \$16 per hour.⁵⁰ Manufacturing wages in Japan, which were about one-quarter of those in the United States in 1970, are significantly higher than those in the United States today.

This progression represents a valedictory to the concept of trading on the basis of comparative advantage. The relatively low wages and eager work force gave Japan, in the early 1970s, a clear comparative advantage in the manufacture of certain goods such as automobiles. Japan was able to offer quality products at relatively low prices. These products appealed to consumers throughout the world and increased demand for Japanese products.⁵¹

As these sales increased throughout the world, there was an obvious concomitant increase in the demand for Japanese labor, an increase which has continually bid up wages and other compensation for Japanese workers.⁵² The increased demand for Japanese labor prompted Japanese companies to invest more time and money into training workers and to purchasing the most up-to-date machinery and technology for these work-

49. See generally Silvia, *supra* note 19, at 634-39, for a discussion of the debate over the passage of the Social Charter.

50. See *supra* notes 32, 39 and accompanying charts.

51. For example, by 1981, Japanese automobile imports represented almost 22 percent of all automobile sales in the United States. See MURRAY L. WEIDENBAUM, *BUSINESS, GOVERNMENT AND THE PUBLIC* 279 (3d ed. 1986).

52. See *supra* notes 32, 39 and accompanying charts.

ers to use.⁵³ This increased dedication to capital investment and worker training made Japanese workers even more productive, enabling them to make even better products. Today Japan has high-cost labor, but that labor is very productive and extremely competitive.

The deregulatory aspects of EC 1992 will make it even easier for goods made in the poorer EC countries to be sold in the wealthier countries. Thus one can expect companies to be even more eager to take advantage of the comparatively low wages these countries offer. From this perspective, the removal of EC-wide trade barriers and other deregulatory aspects of EC 1992 could prove a bonanza for the lesser developed European countries such as Portugal, Greece, and Spain. Indeed, as Charts 1 and 2 illustrate, Spanish workers already have realized sharp benefits as a result of increased foreign investment in Spain during the past two decades. Spanish workers have seen their total compensation package (wages plus formal fringe benefits) increase by approximately 1300 percent during this time period.⁵⁴ This increase is 500-600 percent greater than that which occurred in Germany, Greece, France, and The Netherlands during the same time period.⁵⁵

While the less developed EC nations may not all end up as the next Japan, the same general economic phenomenon which took place in Japan over the past two decades may well take place in these countries. As more companies invest in these countries and more consumers buy their goods, wages will be bid higher. Unlike the sort of Pyrrhic victory which is achieved for workers by way of an edict simply mandating higher wages, real gains in productivity will enable workers to earn better wages over a continuing period of time.⁵⁶

VI. SUBSTITUTES AND COMPLEMENTS

The social dumping fears of Germany, Denmark, and other highly industrialized, high-wage EC countries, really seem to be classic fears of competition and substitution in the context of freer trade.⁵⁷ Their fears are that with the advent of EC 1992, companies will have a greater incentive to "substitute" investment and business in these industrialized countries, with investment and business in countries like Portugal, Greece, and

53. See generally WORLD ECONOMIC FORUM, *supra* note 37, at 73 (ranking Japan number one of all OECD countries in terms of in-company training and compulsory education expenditures). The United States, Germany, and Canada are also part of the OECD.

54. See *supra* notes 32, 39 and accompanying charts.

55. *Id.*

56. See generally KENEN, *supra* note 14, at 13-50.

57. See generally ALCHIAN & ALLEN, *supra* note 45, at 386-92. See also John T. Addison & W. Stanley Siebert, *The Social Charter of the European Community: Evolution and Controversies*, 44 INDUS. & LAB. REL. REV. 597, 617-23 (1991).

Spain. Thus, by raising the cost of doing business in countries that currently have a competitive labor cost advantage, the wealthier, more developed countries hope that competition and substitution will not occur.

These fears, however, are probably somewhat exaggerated, and it seems that countries like Germany should view the production that will go on in places like Portugal and Greece as complementary to their production capacity. The German work force, for example, is extraordinarily well educated and highly skilled. Moreover, Germany has an excellent economic infrastructure and network of suppliers. Thus, while German labor is very expensive, it is also very productive, a fact documented in a recent study comparing wages and productivity among German, French, Italian, and British workers. The study found that while German workers earned as much as 35 percent more than workers in some of these other countries, their productivity was in turn as much as 35 percent higher.⁵⁸ Consequently, high technology companies are going to continue to operate and expand in Germany. Such companies are relatively unlikely to set up shop in Portugal since the workers in Portugal do not yet have comparable education, skills, and training.⁵⁹

On the other hand, workers in places like Portugal can do lower skilled textile manufacturing and other types of work quite successfully. With the removal of trade barriers, which is a goal of both EC 1992 and of the new European Economic Area countries, manufactured goods from countries with low labor costs can be shipped and sold at low prices in Germany. German consumers will then benefit from these low-priced goods, while their productive capacities are utilized in more remunerative endeavors. Thus, Portuguese production can benefit Germany by providing German consumers with lower priced goods. Each country is thus able to specialize in the production of the goods and services it can produce most cheaply. Ultimately, instead of being substitutes for German production, Portuguese manufactured goods may actually end up being positive complements to such production.⁶⁰ In short, the competitive threat of social dumping envisioned by the Germans, Danes, and others may not be nearly as great as it appears to be.

VII. PUBLIC CHOICE ANALYSIS

While the analysis presented above suggests that raising wages and other labor costs by fiat is generally bad economic policy for European consumers and workers, such an approach may be politically correct from

58. Balls, *supra* note 34, at 1.

59. See ALCHIAN & ALLEN, *supra* note 45, at 372-73.

60. See generally *id.* at 373-74 & n.7.

the perspective of certain politicians and interest groups.⁶¹ Thus, political and popular support for the Social Charter and the Action Programme is not entirely the result of misguided economic analyses.

Competition in product markets forces firms to produce as efficiently as possible. This means that increases in product market competition will encourage firms to employ only the most productive workers and pay them wages and benefits that are closely related to the workers' productivity. Firms that employ too many workers, or provide wages and benefits that substantially exceed the value of the workers' productivity, will be unable to price their products high enough in competitive product markets to cover the costs of their labor force. When these firms incur operating losses or earn rates of return that are too low to cover their costs, they must begin to reduce costs if they are to survive. Usually this means reducing the size of their work force as in the case of Renault, whose Chairman, Raymond Levy, predicts a reduction of forty percent in his work force by 1999 if Renault is to compete successfully with Japanese automakers in the European market.⁶²

The long-term effects of such competition will mean better cars at lower prices for consumers and a reallocation of French workers to jobs where their skills will be more valuable, thus expanding France's ability to compete in other product markets. This reallocation of workers will not take place instantly, however, and may last for years or even a decade. It will be painful for all unemployed workers but especially for those who are older. Older workers require the most retraining to be competitive and have the greatest difficulty relocating to other areas where their skills may be in demand.

Unions, business associations whose members enjoy protected markets, and communities where protected firms are located, all have reason to resist the changes that freer trade may bring. Voters in these categories will be losers, at least in the short run. The benefits of reallocating the work force to more efficient uses in the economy will not occur for some time, certainly not before several elections have taken place. Therefore, politicians who represent these interests, who desire to represent these interests, or whose political affiliations are tied to these interests, will have reason to resist the move to freer trade.⁶³

As indicated earlier, those who will benefit the most from freer trade are consumers but they often do not realize how much they may benefit

61. See generally PUBLIC CHOICE AND CONSTITUTIONAL ECONOMICS (James D. Gwartney & Richard E. Wagner, eds., 1988).

62. Renault Sees Need to Eliminate Jobs, N.Y. TIMES, Sept. 21, 1991, at 35.

63. See generally James D. Gwartney & Richard E. Wagner, *Public Choice and the Conduct of Representative Government*, in PUBLIC CHOICE AND CONSTITUTIONAL ECONOMICS, *supra* note 61, at 3, 8-9.

in the future and, even if they do, they are not as well organized politically as unions, business associations, or local community organizations. As a result, these better informed and organized interests often are more effective politically than consumers. The other winners from free trade are those who want to enter the protected markets and trade on the basis of their comparative advantage, but these people usually are from outside the local political district, or the country, and have far less influence on political decision making in the locale or country for that reason.⁶⁴

It is understandable, then, that some of the support for the social dimension proposals is likely to come from those politicians and bureaucrats with ties to organized interests who may be adversely affected in the short run by freer trade. It is also true that those who will benefit the most from freer trade, consumers and workers who will enjoy expanded opportunities, may be under-represented in the political arena because they are not as well organized.

VIII. CONCLUSION

In a recent editorial, *The Economist* pointed out that the European Commission, through its Social Charter and other social dimension proposals may end up killing some of the lesser developed EC countries "with kindness."⁶⁵ This assessment seems correct. By essentially mandating that all European workers be afforded the same benefits and rights as German workers, these proposals are going to end up making workers in countries like Portugal, Greece, and Spain less able to compete effectively. The key comparative advantage these workers have, their low-cost labor, is being taken away from them.

The "freer trade" aspects of EC 1992 will clearly help workers in low-wage countries and benefit consumers throughout the EC. However, there will be adjustments in some countries, as trade on the basis of comparative advantage results in some unemployment in protected industries. It should be noted, though, that such unemployment is most likely to occur in the wealthier EC countries, which have the most extensive social security systems and safety nets to help minimize the effects of unemployment on workers. Some of the proposals being considered as part of the social dimension will clearly have pernicious effects for workers in poorer countries and for consumers in all EC countries. Moreover, they will ultimately reduce some of the potential benefits of a true single market in the EC.

64. *Id.* at 9-10.

65. See *Europe's Social Insecurity*, *supra* note 20, at 13.