Where did all our jobs go?

The Delors White Paper of 1993 sought to create millions of new jobs in Europe before the new millennium. The demand-side and supply-side reasons why it failed could now wreck the euro.

The European Union's employment record is dismal. Since 1970 the US economy has created just under 50 million new jobs, whilst the European Union has created just over 5 million. For every 10 jobs created in the US, only one is created in Europe. Even Japan, despite its economic problems throughout the 1990s, has created more jobs in the last decade than Europe, and by a long way.

This poor jobs performance in Europe has not been a short-term development. It has been a sustained problem which is not about to be reversed, despite the fall in European unemployment during the last year. European monetary union will make Europe's jobs problem worse. Emu stands for 'Even more Unemployment'.

The European Commission and politicians want to create more jobs. This is not the first time. The Delors White Paper of 1993 aimed for 15 million new jobs by the year 2000. The result: employment fell. European policy makers seem unable to tackle the root cause of the jobs problem.

European unemployment is too high, with over 1 in 10 unemployed. Although poor, this flatters the EU, as many people who are not in work do not register as unemployed, for many reasons. The proportion of Europe's working age population which has jobs is low, at only 60.5%. This is lower than in the UK (70.8%), the US (74.0%) and in Japan (74.4%).

There are two reasons for Europe's dismal employment record. On the demand side, excessively tight policies over a sustained time and the deflationary mentality of the exchange rate mechanism and of the Maastricht Treaty contributed to low inflation and allowed 11 currencies to qualify for the euro. For some smaller countries this has brought benefits, but for most it has created problems, leading to weak, below-trend growth, with high unemployment.

In the early 1970s the number of people employed in Europe was on a par with the US. Tight policies had a detrimental impact on European jobs. Unemployment rose through the 1970s and 1980s. Yet even when the EU has grown in the 1990s, unemployment has remained high because of the second reason, the supply-side problem.

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This is structural and explains the inflexibility of Europe's labour market. Regulations, excessive non-wage costs and a higher tax on labour compared with capital have all discouraged firms from recruiting new workers. People may also be inflexible, both in their reluctance to move between sectors and across regions. The supply-side problem has meant unemployment has stayed persistently high, even when interest rates have fallen in recent years.

Workers' rights are important but there is no balance within Europe. The pendulum has swung too much in one direction, so much so that Europe suffers from an insider/outsider problem. Those in jobs are well protected but those outside work find it hard to find jobs. Europe has employment problems for young people, women and men in their 50s, many of whom have been forced to take early retirement. The European Commission is keen to avoid the large wage dispersions seen in the US, but greater US wage flexibility has allowed America to create jobs for lower skilled workers. By contrast, there has been a loss of low skilled jobs across Europe. It would be wrong for the US leaders to gloat, as economic fashions can change quickly, but Europe's problems are deep rooted.

As Europe faces a demand and a supply-side problem this requires a demand and a supply-side solution. The demand-side solution is for economic policies to be geared to creating conditions for growth. The supply-side solution is to ease the burdens on business and reduce high labour costs. The danger is the situation could get worse, not better.

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Emu will not result in convergence across Europe. Regulations and taxes may be harmonised but economic performance is more likely to diverge. Economies of scale within a single market will favour the clustering of industries in particular locations, just as in the US. Economic regions will be very different. Expect significant regional disparities and pockets of high unemployment. This could soon trigger calls for domestically orientated policies across Europe, undermining political and public support for the euro and eventually wrecking the single currency itself. ●

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This is a summary of the Poleteia Lecture given in London on 17 November 1998.