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UNIONS, SOCIAL STRUCTURES, AND WAGE RESTRAINT:
A SUGGESTED SCHEME OF ANALYSIS

Edward J. Amadeo

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Edward J. Amadeo, Associate Professor of the Department of Economics at PUC-RJ, obtained his Ph.D. in Economics from Harvard University in 1985. He has been external consultant for the Brazilian Central Bank, WIDER, PREALC/ILO, the World Bank, and UNRISD. Among extensive publications, he has authored *Keynes's Principle of Effective Demand* (1989) and coauthored, with Amitava K. Dutt, *Keynes's Third Alternative? The Neo-Ricardian Keynesians and the Post-Keynesians* (1990) and, with Marcello Estevão, *A Teoria Econômica do Desemprego* (1991). He is editor of *John Maynard Keynes: cinquenta anos da Teoria Geral* (1989) and *Ensaios sobre Economia Política Moderna* (1990). He is currently completing a book on '*New Unionism,' Collective Bargaining, and Distributive Conflict in Brazil*.

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ABSTRACT

The aim of this paper is to provide an overview of the literature on the relation between institutional aspects of wage bargaining and stabilization policies. The paper starts with a discussion of the logics of unions' attitudes in wage bargaining in an attempt to highlight the costs and benefits associated with wage restraint. Next, it relates the conditions of wage restraint to the literature on union movement centralization, trade dependency, workers' militancy, neocorporatism, and stabilization policies. We then create a taxonomy of industrial relations systems, and identify two "ideal cases"—the corporatist and pluralist cases—and two "hybrid" cases. We conclude that certain hybrid characteristics have a potential to generate ustable macroeconomic outcomes, and to render particular economic policies either infeasible or ineffective.

RESUMEN

El objetivo del presente trabajo es presentar una revisión general de la bibliografía sobre la relación existente entre los aspectos institucionales de la negociación salarial y las políticas de estabilización. El trabajo comienza con una discusión sobre la lógica de las actitudes de los sindicatos en la negociación salarial, en un intento por destacar los costos y beneficios asociados con la moderación salarial. Enseguida relaciona las condiciones de la moderación salarial con la bibliografía sobre el grado de centralización del movimiento sindical, de apertura y dependencia comercial de la economía, la militancia de los trabajadores, el neocorporativismo y las políticas de estabilización. Esta discusión nos conduce a presentar una taxonomía de los sistemas de relaciones industriales, y a identificar dos "casos ideales"—los casos corporativista y pluralista—y dos casos "híbridos". Llegamos a la conclusión de que ciertas características de los casos híbridos pueden potencialmente generar resultados macroeconómicos inestables y volver impracticables o inefectivas ciertas políticas económicas.

1. INTRODUCTION

Since the mid-1970s increasing attention has been dedicated to the institutional and structural factors affecting the determination of money wages in both the political science and economics literatures. By the late ’60s, the “golden age of capitalism,” characterized by high levels of investment, growing productivity and consumption per capita, and stable prices and distributive shares in the advanced OECD economies, seemed clearly over (see Lipietz et al. 1990). The slowdown of productivity and the oil shocks of 1974 and 1979 made the trade-off between inflation and unemployment—the Phillips curve—more stringent. Over the 1970s and ’80s, there was a marked deterioration in the performance of all economies, albeit some diversity in national experiences (see Rowthorn and Glyn 1990). Wage restraint has been seen as a major ingredient in explaining the relative success of certain economies in coping with the crisis (see Bruno and Sachs 1985). In countries in which the unions’ attitudes are conductive to wage restraint, the macroeconomic performance (as measured by some combination of inflation and unemployment) has been clearly superior to the performance of those in which union militancy and wage demands have not diminished.

The notion that labor market institutions matter in shaping macroeconomic outcomes has become quite widespread. The huge literature on unions’ and employers’ associations, patterns of wage bargaining, concerted incomes policies, neocorporatism and pluralism, and macroeconomic performance has been able to divert (at least some) economists from simplistic, institution-free approaches to the problems of unemployment and stabilization. Orthodox economists have learned from and indeed contributed to this literature, and in a sense, have created the possibility for a Keynesian comeback (see Bruno and Sachs 1985 and Blanchard and Summers 1986).

The aim of this paper is to provide an overview of this literature in order to discuss the relation between institutional aspects of wage bargaining and stabilization policies. The paper starts with a discussion of the logics of unions’ attitudes in wage bargaining in an attempt to highlight the costs and benefits associated with wage restraint. Next, it relates the conditions of wage restraint to the literature on union movement centralization, trade dependency, workers’ militancy, neocorporatism, and stabilization policies. We then create a taxonomy of industrial relations systems, and identify two “ideal cases”—the corporatist and pluralist cases—and two “hybrid” cases. We conclude that certain hybrid characteristics have a potential to generate unstable macroeconomic outcomes, and to render particular economic policies either infeasible or ineffective.

2. STRUCTURAL AND INSTITUTIONAL DETERMINANTS OF WAGE RESTRAINT

In principle, unions act in the name of their members and have to confront employers on the bargaining table. In addition, they have to take into account the economic policies of the government in making their demands, and in certain cases the orientation of confederations and political parties. Unions leaders have to ponder over the objectives and interest conflicts of these different groups in making their decisions concerning wage demands. They also have to take into account their own interests as a group which implies preserving their legitimacy by being loyal to the members and keeping their credibility with the opposing negotiating parties. In the following section we look at the logics of unions' attitudes in wage bargaining, and try to picture union leaders as pivotal agents in this network of interest accommodation.

2.1 The Logics of Unions' Attitudes in Wage Bargaining

We may take as a starting point the objective of an union when negotiating the determination of money wages (w). Depending on the circumstances, unions will have different objective functions. In economies in which the monetary and fiscal policies are accommodative, that is in which the government and central bank recurrently accommodate inflationary pressures with the aim of keeping low rates of unemployment, unions may well concentrate on maximizing the real wage of their members. However, in general, we may assume that some degree of trade-off exists between the real wage and the level of employment in which case unions will look at the real wage bill rather than the real wage as their target variable. Accordingly, we assume that unions try to maximize the real income of their members as represented by:

$$\max_{w} \ (w/p).L$$

where p is the price level, w/p is the real wage, and L is the level of employment. In maximizing its members income, the union faces a variety of uncertainties and constraints:

[A] Two elements that the union might take into account are the impact of the increase in money wages on the aggregate price level (or on inflation) and the reactions of the government to reduce inflation which may hurt labor. If firms are assumed to (at least partially) markup costs, an increase in money wages will create inflationary pressures which in turn will to a greater or lesser extent negatively affect the real wage. On the other hand, unions might be aware that in certain circumstances the acceleration of inflation brings about pressures to adopt deflationary policies—with undesired effects on employment. These two "boomerang effects" may constrain the attitudes of the union.

[B] The union will certainly face opposition from the firm or group of firms with which it is negotiating. Firms have a basic joint objective: to increase as much as possible the profit per unit sold (profit margin) and the number of units it can sell. The product of the two determines the amount of sales proceeds, and given the costs of production, the level of profits. There is a clear trade-off between the two objectives mentioned, that is, the greater the profit margin, the smaller the size the of clientele. Firms try to maximize profits (sale proceeds net of costs), and hence, given the market constraints, will obviously resist increases in wage costs. The goods market poses a constraint for the firm, and the greater the constraint, the greater the willingness of the firm to resist wage increases, and to impose conflict costs on unions.

[C] Finally, the bargaining power of the union depends on the support it has from its members. Here it is important to differentiate between the union and the union members (workers), on the one hand, and between militancy and bargaining power, on the other hand. The union negotiates in the name of the workers, and must therefore represent their interests. If it does not, it loses bargaining power for it lacks support for its actions. Militancy and labor mobilization only enhance the unions' bargaining power if unions and workers have the same purposes and agree on the strategies. Wildcat strikes are a good example of situations in which the level of militancy is very high, but the union has lost control over the workers (owing to differences in either purposes or strategies), and also the right to speak in their names, in which case its bargaining power is obviously very small.

Constraints A, B, and C are affected by a number of structural, institutional, and conjunctural factors to which we now turn. In terms of the first constraint, the following factors seem to be of some relevance:

[A.1] The impact of wage negotiations on inflation obviously depends on the "size" of the negotiating party. The greater the degree of centralization of negotiations, and hence the relative size of the negotiating party and weight in the formation of the aggregate price level, the greater the inflationary effect of wage increases.

[A.2] The real wage of a certain group of workers depends as much on their money wage as on the money wages of other workers in the economy. For the greater the increase in money wages in other sectors, the greater will be the average price level, and the lower the real wage of the group under consideration. Hence the union must take into account the (expected) level of wages in other sectors when negotiation its own money wage.[1] The degree of *synchronization* in the formation of wages in the economy plays an important role in shaping the attitude of unions and workers for the greater the degree of dis-synchronization, the greater the uncertainty concerning the level of wages in other sectors. When uncertainty is large, and the risk of falling behind the average is thus large, workers try to protect the purchasing power of their future income by augmenting their demands for wage increases. When wages are set in synchronous fashion (which is

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[1] The notion that relative wages are the real concern of unions was first put forward by Keynes in his *General Theory*. There he argued that "the struggle about money/wages primarily affects the *distribution* of the aggregate real wage between different labour-groups, and not its average amount per unit of employment, which depends...on a different set of forces. The effect of combination on the part of a group of workers is to protect their *relative* real wage" (1936, p. 14).

usually the case when the degree of centralization is high), or a certain sector plays the role of a "pattern setter," the level of uncertainty is reduced, and the incentives to take precautionary measures diminishes.

[A.3] No matter how centralized and synchronized negotiations actually are, and the effect on aggregate inflation of wage increases in a given sector actually is, the attitude of the union will only be influenced by this factor if it realizes or if it is *aware* of the consequences of the wage bargain. Of course, the greater the size of the union, the greater the likelihood that it will be aware and hence consider the macroeconomic effects of its activities. In particular, in countries in which negotiations take place at very high levels, union leaders are clearly aware of the aggregate impacts of wage negotiations. They tend, therefore, to internalize the costs of the externalities created by the negotiations. Small unions, on the other hand, usually are not aware of the macroeconomic impacts of their demands.

In terms of the second constraint (B), or the goods market constraint,

[B.1] It is reasonable to assume that the elasticity of demand of the negotiating firms falls as the level of centralization of negotiations increases at the industry level. Firms can enter into collusive action and clients have a smaller number of substitutes to chose from as the level of centralization increases (see Calmfors and Driffill). This obviously implies that the market constraints become less stringent as the degree of centralization increases, and that firms' willingness to engage in conflict with workers falls.

[B.2] Whether we look at a particular industry or at a national economy, the size of the market constraint will depend on the level of protection from external competitors and the degree of trade dependence (that is, necessity to export). Protected and/or domestic-oriented industries face smaller market constraints than unprotected and export-oriented industries.

We finally turn to the third set of constraints (C) associated with the labor organization and incentives for workers' militancy:

[C.1] The degree of centralization of the labor movement may be an important factor in shaping unions' attitude in wage bargaining. Ceteris paribus, smaller unions are weaker than large unions. Industry unions control the supply of labor to a set of firms and have more power than firm unions. The centralization of the union movement increases its bargaining power. This is not meant to deny the fact that certain small unions in decentralized systems may be very powerful. The argument is only that the bargaining power of a (legitimate) union tends to be greater the greater the number of its members. The existence of active central unions that support industry and local unions in their negotiations, and maintain ties with political parties represents yet another important element in understanding the conditions of wage restraint.

[C.2] Policies that protect the workers' income from shocks or the conditions of the economy—or, in short, insulate the workers' income from market fluctuations—tend to reduce labor militancy. In advanced OECD economies, and in Western Europe in particular, the increase in social spending, or the increase in the "social wage," has been seen as a response to labor militancy, as well as an important factor in taming labor militancy. In the case of inflation-prone economies, wage laws have an important role in protecting real wages against inflation. If the policy is effective in protecting wages, the incentives for mobilization during bargaining periods are reduced. Both the degree of indexation to past inflation and the length of the indexation period are important in determining the effectiveness of the wage policy. Low degrees of indexation and long indexation periods imply great vulnerability of wages to inflationary shocks, and thus create incentives for mobilization and conflict.

[C.3] Instability is also a factor to be considered. When recent history is marked by recurrent inflationary shocks, changes in policies and rules of the game, leading to erratic movements of the real wage, there is an incentive for workers to take preemptive actions during negotiations. Such actions aim to increase wages as an insurance against shocks at the cost of more mobilization.

[C.4] Finally the conditions of the labor market as represented by the rate of unemployment negatively affects the level of militancy and the capacity of unions to mobilize workers, thus reducing their bargaining power.

2.2 Conditions for Wage Restraint

The discussion in the previous section provides a guide for the analysis of the factors accounting for wage restraint. National experiences are the outcome of a myriad of interrelated factors, but some of these factors are certainly more salient than others. Comparative analyses of national experiences in which outstanding factors are highlighted have proved to be instructive exercises. The analysis of the unions' aims and attitudes under different circumstances is used in what follows to sort out the alternative "ideal cases" discussed in the literature on industrial relations and macroeconomic performance. The ideal cases can be seen as resulting from the combination of certain conditions associated with different subsets of constraints to the unions' actions. Table 1 summarizes these conditions.

TABLE 1

	Conditions for Wage Restraint
[A.1+A.2+A.3]	Negotiations at national or near-national level and/or high degree of synchronization in wage setting
[B.1+C.1]	Small unions and decentralized/localized negotiations
[B.2+C.4]	Trade dependency and (threat of) unemployment
[C.2+C.3]	Insulation of workers' income from shocks and market fluctuations; stable rules of the game and government/employers' credibility

A careful analysis of the Table reveals certain inconsistencies among the sets of conditions. In particular, there is a clear contradiction between the two first conditions, that is, [A.1+A.2+A.3] and [B.1+C.1]. The two sets of conditions are associated with two different industrial relations paradigms, namely, the societal corporatist and the pluralist paradigms, respectively.

The other two sets of conditions qualify the first two.

2.2.1 Societal Corporatism

The notions of societal corporatism (Schmitter 1971) and neocorporatism (Crouch 1985b) are rather diffuse.[2] They involve different aspects of interest representation including the degrees of centralization of the union and employers' movements and of collective bargaining, relations between the labor movement and political parties, and participation of labor leaders in government. However, an outstanding underlying argument in favor of the cooperative behavior of agents in corporatist systems is that the smaller the number of powerful players in the political market the greater the damages that individual groups can inflict on others, and therefore the greater the incentives for cooperation. The obstruction capacity of the groups, and the detrimental aggregate or social effects of each group's actions, are so huge that the benefits of cooperation increasingly dominate the costs of conflict. Not only that, but some would also argue that by exploring the gains of cooperation, agents could also transform a "zero-sum game" into a "positive-sum game" (Korpi and Shalev 1979, p. 172).

In the industrial relations arena, in most of the countries that today constitute the representatives of the ideal corporatist case, "the massive conflict (between workers and employers) that characterized centralized systems" was replaced by cooperative actions aiming at long-term goals that are seen as beneficial to both groups. The centralization of the union movement, which in most European countries took place after the First World War, can be seen as an attempt of union leaders to expand their bargaining power in the political market.[3] The consequences of the political action of centralized workers' movements are appreciable: the participation of labor representatives in political parties and the government and the adoption of normative interventions of the State in labor relations, such as the establishment of minimum wages, maximum working hours, unemployment benefits, and social security schemes, are the most prominent examples.

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[2] For a critique of the notion of corporatism and its association with macroeconomic performance, see Therborn (1986).

[3] Pizzorno (1978, p. 286) notes that "on the side of unions, the creation of central bodies (federation, confederation, national council, Bund, etc.) may be considered an elementary indicator of the emergence of a situation which implies exchange between political actors."

As a result of the participation of organized labor in the political market, and indeed in local and national governments, cooperative rather than conflictual relations between unions and employers have developed. To be sure, a major exchange between workers and employers has anteceded the inauguration of the cooperative system—an exchange of workers' protection against market fluctuations for lower militancy. The attainment of long-term goals at the cost of short-term sacrifices is also seen as a consequence of the "social-democratic pact."

Centralized and synchronized wage bargaining is also seen as an important characteristic of corporatist systems and indeed a major factor—together with the cooperative compromise—in explaining wage restraint. In this connection, the social bounds imposed on agents' attitudes by a particular institutional arrangement, namely, centralized bargaining, is very important. The combination of constraints A.1, A.2 and A.3 is central for the explanation of wage restraint in corporatist systems: because the bargaining parties have a "socially relevant size" their attitudes have an immediate effect on aggregate variables.[4] Immediate or individual gains have to be weighed against the medium- and long-term and social losses. In the case of fully centralized and synchronized bargains, the intertemporal net gains become clearly perceived by the agents, who therefore act accordingly. Where negotiations are only centrally coordinated or parallel but decentralized bargains may give rise to wage drift, depending on the sizes of the second and third tiers negotiating parties, the net intertemporal effects might *not* be taken into account because agents may not be aware of the losses, or have difficulties in accessing them. Where negotiations are decentralized and/or scattered over time, and the negotiating parties are small, the level of awareness will tend to be small.[5]

Much ink has been used to provide empirical evidences that the corporatist system (crudely typified by centralized union organization *cum* centralized/synchronized wage bargaining) is conductive to wage restraint. To summarize the central arguments we consider the works of Crouch (1985b) and Cameron (1985).[6] The common aspect of these analyses is an attempt to show that diversity in economic performance among advanced OECD economies after the mid-1970s is closely correlated to industrial relations institutions.

Crouch's central argument is that the relation between union density and inflationary pressures must be mediated by institutional variances; and that the record of corporatist

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[4] The argument is put forward by Crouch as follows:

> Social interests that are organized on a small, localized scale receive in full any gain from distortions they produce in market processes but bear only a minute proportion of the general cost... The position of an organized interest at a national or near-national level will be completely different, as it will experience directly the negative effects of its disruptions—it can therefore be expected to take these effects into account (1985b, p. 107).

[5] However, as we shall note in the next section, other bounds to the agents' behavior apply.

[6] In the economics literature, Bruno and Sachs (1985) come to conclusions that in essence are very similar to the ones of Crouch and Cameron.

countries[7] with respect to the relation between unionization and inflation (and the Phillips curve trade-off) is superior to that of pluralist systems. Crouch summarizes his findings with respect to wage restraint as follows:

> the extraordinary rise in inflation during the mid-1970s, as well as the difference among national rates of price acceleration, is better explained by industrial relations forces than just by prior inflation alone. This is compatible with the hypothesis that organized labor used its strength to secure short-term protection from the commodity price shocks, except to the extent that neo-corporatist structures led it to pursue strategies more compatible with longer-term price stability… Where there is social consensus (which might be secured by corporatist institutions) there will be relatively rapid adaptation of real wages to economic developments, and therefore less inflation (pp. 124-5).

The work of Cameron (1985) attacks the dominant view according to which there exists a trade-off between inflation and unemployment. He uses a cross-country correlation analysis to show that, contrary to the conventional wisdom, among advanced industrial countries, those in which the acceleration of inflation was smaller were also the ones in which unemployment did not increase significantly after the oil shocks of 1974 and 1979. Also, he shows that money wage inflation and real wage increases took place where the degree of workers militancy (as measured by strike activity) was greater. The conclusion is that real wage restraint is positively associated with low levels of militancy, money wage and price inflation, and unemployment. Cameron further argues that corporatist institutions—e.g. organizational unity of the labor movement and an important role ascribed to central unions in wage bargaining—and dominance of leftist parties in the government are the common features of countries with the best macroeconomic record.

2.2.2 Pluralism

The pluralist ideal case is best portrayed by the “competitive system” that plays a paradigmatic role in the neoclassical economics literature. Where agents are too small to affect the market, the forces of supply and demand at the industry level fix the money wage and price of output. In the idealized atomistic system, firms are small and take the price of the goods they produce as given. Faced with a given price, and with a money wage determined by supply and demand for labor at the industry level, the firm fixes the optimal levels of output and employment. The interaction between the actions of the individual agent and the market forces that ultimately determine prices is not spelled out in the competitive paradigm. Indeed, this is a widely recognized weakness of the model which relies on the figure of a ghost called the “Walrasian auctioneer” to collect demands and supplies of millions of agents, to eventually through a trial and error process determine the competitive equilibrium prices.

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[7] Austria, Denmark, Finland, the Netherlands, Norway, Sweden, Switzerland, and West Germany.

In order to make sense from an empirical perspective, the competitive system has to be modified. In the economics jargon, a certain degree of "imperfection" must be introduced. The demand curve faced by producers (an individual firm or a group of them producing similar goods) is not perfectly elastic and certain oligopolist factors such as fewness and product differentiation are taken into account. These modifications imply that a certain degree of discretion in the formation of prices is allowed for. In the labor market, labor segmentation due to differences in general abilities and specific skills as well as factors influencing the bargaining power of unions, lead to modifications in the outcome resulting from the forces of "supply and demand" or the "auction market."[8] The determination of wages and prices will ultimately depend on the goods market constraints (or firms' degree of freedom to alter prices) and the bargaining power of the union and the firm(s).[9]

Where wage bargains take place at very decentralized levels, the power of confederations and federations is negligible, and direct negotiations between local unions and the firm are the ultimate determinants of wages. Under these circumstances, conditions B.1 and C.1 hold, and wage restraint results from the fact that competitive pressures put a cap on price and wage increases. In pluralist systems, therefore, the market imposes bounds on individual agents' actions.

Faced with an adverse shock, like the oil shocks of 1974 and 1979, or productivity slowdowns, which tend to reduce the demand for labor, economies with pluralist institutions would respond with brisk real wage moderation. As a result, neither inflation nor the level of unemployment would suffer considerable increases. According to empirical analyses conducted by Bruno and Sachs (1985) and Klau and Mittelstadt (1986), real wage flexibility in the case of the US, for example, resulted not only from the decentralized and disynchronized pattern of wage bargaining, but also from the fact that there is a low degree of unionization and a "rapid inflow into

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[8] These modifications do not alter the essence of the pluralist paradigm which is that small negotiating agents have small market power. Price and wage differentials resulting from different market structures have been the object of study of economists since the 1930s after the pioneering works of Sraffa (1926). Robinson (1939).

[9] There are other characteristics of the pluralist system that deserve special attention. One is that because agents are small they do not care about the (small) aggregate effects of their actions. The other characteristic does not really stem from the ideal case itself but it is observable in countries in which other pluralist features exist, and that is the low level of politization of the agents. Not only are the links between the unions and federations weak, but the ties between the union movement and parties are also very thin. Crouch describes as follows the pluralist ideal system:

> (atomized) actors do not take action with regard to any perception of a general interest; the market impersonally imposes on them conformity with a general interest. Further, as economic actors they are confined to acting within the sphere of economic relations, producing and exchanging goods and services in order to realize a goal of profit maximization. They have no concern for general political questions, and no sense of group or common interest (Crouch 1985b, p. 108).

the labour force of young persons and women prepared to accept employment at low wages" (Klau and Mittelstadt, p. 25). The low degree of wage indexation to inflation and the presence of multiyear contracts are repeatedly mentioned as important factors as well.

Flexible wage differentials also account for rapid adjustment to shocks which hit different sectors with different strength. Again, in empirical studies it has been found that the degree of relative wage flexibility is greater in the US than in European countries, and it has been argued that this could explain the greater degree of real wage flexibility (see Klau and Mittelstadt). Bell and Freeman (1987) have noted however that although it is true that the US is unique in this respect—indeed, it is the only OECD advanced economy in which sectoral wage dispersion has increased—relative wage flexibility has not really worked to generate more employment. The increase in wage dispersion is associated with industry-specific conditions and not with changes in the sectoral patterns of demand and supply for labor. Quite contrary to expectations, wages have been growing in sectors in which productivity has gone up and falling (though not as much) where productivity has been falling. As a result, the net effect of the increase in wage dispersion cannot be seen as positive factor in increasing the level of employment.

2.2.3 Intermediate and Hybrid Systems

The corporatist and pluralist systems discussed are really limit-cases, and can be seen as two poles of a spectrum on which other relevant systems exist. The "hybrid cases" preserve some of the characteristics of the pure cases, but at the same time present certain distortions. In what follows we address three sources of modifications to the pure cases, and then build a taxonomy of systems based on two attributes: the level of centralization of collective bargains and the degree of synchronization of wage negotiations.

The three modifications to the pure cases are the following:

[i] The typical level of negotiation may be intermediary between the firm and the economy as a whole. When bargains take place at high levels of aggregation at the industry level, or at the industry level itself, some special features arise. As the size of the negotiating party increases, the elasticity of demand falls because the "good" now comprises a wider range of substitutes (see Calmfors and Driffill 1988). Not only that but the possibility of collusion increases the firms' market power. On the other hand, the bargaining power of the union(s) tends to increase in direct relation to the

> size of the labor supply that it controls.[10] The slackening of the market constraint, and resulting increase in the market power of firms, and the increase in the bargaining power of unions, tend to reduce the bounds of wage (and price) increases.[11] From the point of view of the pluralist paradigm, the increase in the level of aggregation of negotiations at the industry level introduces an injurious "imperfection" in the system.

In terms of the corporatist system, the reduction in the level of bargaining (in relation to the centralized system) is also damaging for it reduces the level of awareness of the agents concerning the aggregate consequences of their actions.

From a comparative perspective, therefore, the intermediate case is inferior in relation to both the pluralist case and the corporatist case. Industry level negotiations are seen as conductive to wage inflation and price inflation.

> [ii] Decentralized negotiations do not necessarily imply disynchronization for bargains may occur simultaneously. On the other hand, where centralized bargaining exists, there is space for the effects of assynchronicity as second and third layer negotiations usually coexist with economy-wide bargains. In sum, conditions A.1 and A.2 do not mutually imply each other, and hence another source of variation with respect to the two pure cases is the possibility of "centralized but assynchronic" and "decentralized but synchronic" negotiations. The former is in fact implicit where corporatist institutions predominate.

Both centralization and synchronization are seen as important coordinating instruments and factors accounting for wage restraint. The gains stemming from centralization have already been discussed. Synchronization in turn mitigates the level of uncertainty concerning the future path of wages in different sectors of the economy, and hence reduces the incentives for unions to take preemptive actions against possible reductions in real wages. It is important to note that

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[10] The change in the elasticity of demand as negotiations become more centralized is spelled out in detail by Calmfors and Driffill (1988, p. 33):

> As unions get larger, they acquire greater market power. In an individual firm, workers have little market power. Indeed, any isolated increase in the nominal wage results in a large employment fall, since the firm is unable to raise its output price unless all firms within the industry do so. But, if the union were to control labour supply to all firms in the industry, its market power would grow. Indeed, each firm within the industry has the same incentive to raise its output price which, therefore, rises in the whole industry. Substitution now occurs only in relation to firms outside the industry, and no firm faces a fall in demand relative to other firms in the same industry.

[11] Crouch provides an interesting view of the relation between the market power of firms and the limits of wage increases:

> It is within oligopolies and in the public sector that unionization in most countries is strongest; and in these sectors unions are able to bid up wages, not entirely independently of the overall level of unemployment but with considerably less dependence than in a perfectly competitive system. Within the oligopolies, unions have thus been able to preempt for labor at least some of the fruits of market power produced by the concentration of industry, leading either to profit squeeze or, as prices finally rise, inflation (Crouch 1985b, p. 107).

neither centralization nor synchronization are sufficient conditions to prevent nominal wage increases. Wage drift can occur in both cases when the pattern set by the nation-wide bargain or a pattern setter, respectively, are not respected in local negotiations.

[iii] The role of central unions or confederations in collective bargaining also affects the system of industrial relations. Two aspects seem important in this connection. The first is the extent to which confederations participate in bargains. In some countries the participation is negligible if it exists at all; in others they play the role of a consulting agent in providing the negotiating unions with advice and expertise; in others they negotiate in the name of the unions. In the first and second cases the power of the central unions is limited but in the third case unions may not have the right to renegotiate at the local or plant level issues negotiated at higher levels.

Another important aspect refers to the degree of centralization of the union movement and the bargaining process. Where a single confederation exists the prospects of concerted policies, and hence macroeconomic coordination, are greater. Where more than one confederation exists, and the cleavages are political, the actions of central unions may be rather disrupting, not only because of differences in strategies but also because it makes tripartite accords much more difficult. Where the confederations are weak and insignificant, their overall role in collective bargaining is negligible, and the prospects of concerted policies are nonexistent.

Table 2 is an attempt to take stock of the previous discussion. It considers two attributes of wage setting negotiations, namely, the degree of centralization (high, intermediate, and low) and the degree of synchronization (high and low). High degrees of centralization and synchronization characterize the corporatist system whereas the symmetric case characterize the pluralist system. High and negligible degrees of unification of the union movement, respectively, are implicit in the two limit cases.

TABLE 2

Patterns of Wage Bargains

		Level of Centralization		
		High	Intermediate	Low
Level of Synchronization	High	Corporatist	Hybrid I	***
	Low	***	Hybrid II	Pluralist

There are two hybrid cases of some interest. In the hybrid I case, the degree of centralization of negotiations is intermediate (or low) but the degree of synchronization is high—thus providing a significant coordinating element to the system. The role of pattern setters is important in this system. In hybrid II, the predominant level of negotiation is intermediary and the degree of synchronization is low. This is a system with very problematic features because all the coordinating mechanisms are absent.

Over the 1980s a general trend towards decentralization of negotiations has been noted in all advanced industrialized countries. The requirements of greater flexibility of wages and labor processes in face of new developments in technologies and of the economic crisis have led employers to push for decentralized bargains. The tendency is much clearer in the US and UK than in other countries.[12] Where a tradition of relatively centralized negotiations (either at the industry level or at the national level) exists, the change has been much slower. In fact, industrial relations institutions have shown an impressive degree of inertia even in face of employers' and some governments' attempts to change them (see Treu, 1987).

The slots in which Sweden, Austria, Finland, Denmark, Norway, on the one hand, and the US and Canada, on the other, fit in the Table is incontrovertible. The first group forms the core of the corporatist system, whereas the second is distinctively pluralist. More difficult to classify are the cases of the Netherlands, Belgium, West Germany, Italy, France, the UK, and Japan. In order to illustrate the hybrid cases we shall direct our attention to Belgium, France, and Japan.

Japan is usually seen as a typical pluralist case. Calmfors and Driffill (1988, p. 16) for example contend that "as to Japan, there are several national confederations of labour but their coordinating roles are minor, and the actual negotiations take place exclusively at the enterprise level." It is quite true that the confederations play a minor role and that, ultimately, negotiations take place at the firm level, but there are two characteristics of the Japanese system that differentiate it quite dramatically from the American and Canadian systems. On the one hand, the role of pattern setting is very important in establishing the guidelines for negotiations. On the other, there is a preparation involving major industry-level federations for what is called the spring wage offensive (Shunto) in which macroeconomic issues and other national themes are taken into account. More important, however, is the fact that all negotiations take place around a certain period, that is, the degree of synchronization is extremely high.

The decentralized nature of collective bargaining in Japan has been greatly over-emphasized in the literature. Again, although it is true that formal negotiations take place at the enterprise level, intense informal negotiations at higher levels seem to play a decisive role in

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[12] The role of employers in reducing unions' membership and replacing collective bargaining by individual agreements is particularly prominent in the US—see Freeman (1989).

TABLE 3

		Hybrid Cases	
	Belgium	**France**	**Japan**
Unemployment[a]	11.0	7.2	2.2
Inflation[b]	7.6	12.9	5.2
Okun Index[c]	17.0	16.9	9.1
Strike activity[d]	156.0	278.0	71.0
Scope of wage bargaining	Interm.	Interm.	Interm.
Synchronization of wage bargaining	Low	Low	High

[a] Percentage of labor force, average 1980-82. Source: Cameron (1985).
[b] Annual, 1980-82. Source: Cameron (1985).
[c] Okun "misery index" is the sum of the rates of unemployment and inflation, in this case the average levels between 1974 and 1985. Source: Calmfors and Driffill (1988).

shaping local agreements. Employers and union confederation leaders meet frequently with government officials to exchange views on major national issues. Industry-wide federations of enterprise unions not only establish the guidelines for local negotiations, but indeed, as noted by Shirai (in Windmuller et al. 1987, p. 243):

> in *de facto* negotiations the representatives of industrial federations of unions do not act as bargaining agents for the affiliated enterprise unions, but negotiate annual wage increases informally and directly with the top management of leading corporations. The most typical case is that of the centralized bargaining practiced since 1959 in the steel industry between the leaders of the Japanese Federation of Iron and Steel Workers' Unions (*Tekkororen*) and the management of the five major steel corporations... This has become the normal method of wage fixing in the iron and steel industry and has set the pattern for the wage settlement procedure followed in some other major industries.

Shirai also notes that the leadership of the *Shunto* offensive is dominated by the federations of the iron and steel, shipbuilding, automobile and electrical appliances industries, and that although the role of the National Joint Committee for the Spring Offensive is informal, the bargaining with employers' representatives:

> has practically the same effect as more systematic procedures of industry-wide or multi-industry negotiations since the industries concerned are closely related and exert a decisive influence on wage settlements in other branches such as chemicals, metal engineering, private and national railways, telecommunications, and postal services, and national and local civil services (p. 244).

The guidelines are usually followed at the enterprise level. At the industry level, in general the leading firm sets its wage, and the others tend to follow the leader because this at the same time saves bargaining costs and is in accordance with the principle of “wage justice” (see Takanashi, p. 15).

It seems that to place Japan among the pluralist countries is very misleading. Indeed, in doing so the important coordinating elements of the Japanese system, namely, pattern setting and synchronization, are relegated to a secondary status, and the compliance of local negotiations with the guidelines established at higher levels comes to be seen inaccurately as a consequence of “smallness” and market forces.

In France, the level of synchronization of wage bargains is very low which implies that the conditions for coordination in this respect are nonexistent. As for the level of wage bargaining, it usually takes place at the industry level for fixing guidelines—which becomes the minimum level—and then renegotiations at the enterprise level determine the actual wage.[13] Another aspect of the French case that deserves attention is the role of central unions, split on political lines, which tend to act independently from each other and from the government, thus reducing the level of standardization and coordination of the system. This is the typical case in which a few powerful agents without much commitment to the aggregate consequences of their acts can create significant economic and even social disarray. In such cases, neither coordination through concertation nor the discipline imposed by the impetus of the market seem to impose wage restraint.

In Belgium, negotiations take place at different levels depending on the industry: at the national interindustry level (until 1975), at the national industry level, and at the regional and enterprise levels. High level negotiations usually set minimum standards which can be renegotiated at lower levels. However, after the mid-1970s, as a result of the economic crisis that hit the Belgium economy very strongly, interindustry negotiations have not been concluded.

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[13] Caire (in Windmuller et al. 1987) notes that as for the negotiation of wages, “collective bargaining...is conducted at the industry level, the general practice being to negotiate only minima which enterprises, by unilateral decision, may exceed” (p. 201). However, there are variations according to the sector:

> At the level of industry-wide negotiations...complete disorder reigns. Some industries negotiate at the national level (chemicals and textiles, for example) but others prefer the local level and rule out any national agreements (e.g. metalworking). Sometimes (as in the construction industry) the national agreement explicitly relegates some matters—including wages—to supplementary local agreements. At other times, wage scales are determined at the national level with perhaps some local codicils being added later (p. 200).

Blanpain (in Windmuller et al. 1987) points out that "as a consequence of the crisis, the difference between the stronger and the weaker sectors of the economy has become more pronounced, so that an overall agreement under which the trade unionists in the stronger sectors risk losing their comparative advantages has become a less realistic proposition" (p. 183). In some industries (such as textiles, insurance, and retailing) national agreements are still the rule, but in others (metalworking) local agreements have prevailed.

Much as in the French case, in Belgium there are different levels of bargaining depending on the industry, and negotiations have obviously not been synchronized. As a response to the lack of negotiations at the interindustry national level, and increasing reduction in the degree of coordination, since 1981 the government and the parliament have imposed mandatory restrictions on wage increases, which have led to a certain degree of real wage moderation, indeed real wage reductions in some years. Since then, collective bargains have been restricted to other issues among which the reduction in work time and job security are prominent.

The cases of Japan, Belgium, and France are illustrative of the fact that differences in the levels of negotiation and synchronization of wage setting give rise to interesting hybrid cases. In Japan, negotiations formally take place at the enterprise level but informal negotiations at higher levels, pattern setting and synchronization play an important part in the determination of the actual level of wages. In France and Belgium, negotiations take place at different levels but the role of interindustry negotiations has been eroded by the crisis in the last ten to fifteen years and the degree of synchronization and pattern setting is very low. These differences tend to imply that the potential for wage restraint in Japan is considerably greater in Japan than in the two European countries, and the facts confirm this hypothesis.

Both Calmfors and Driffill (1988) and Freeman (1989) argue that there exists a hump-shaped relation between the degree of centralization of negotiations and wage restraint. The conditions for wage restraint hold either when negotiations take place at a very high level or a very low level. Intermediate systems are bound to excessive wage increases and, hence, a severe trade-off between inflation and unemployment.[14] The hump-shaped pattern results from a lack of coordinating mechanisms at intermediate levels of bargaining.

We would argue that there are other factors accounting for the degree of coordination and wage restraint. As noted above, the degree of synchronization of negotiations or the existence of pattern setters affect the level of coordination. If negotiations take place at the

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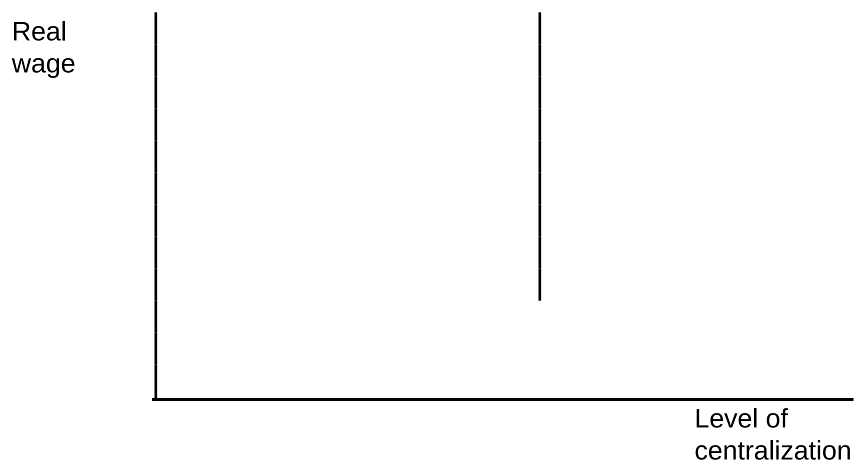
[14] In face of the recent trend towards decentralization, the following argument put forward by Calmfors and Driffill (1988, p. 47) calls for some degree of prudence:

> The main point remains that what one should not do is to go only part of the way to a somewhat more decentralized system with, say, industry-level bargaining. In economies with wage setting at this level one should not resist tendencies to enterprise bargaining in order to preserve some coordination.

industry level (such as we would argue is the case in Japan) but the degree of synchronization is high, the level of coordination will be greater than in cases in which wage bargains are scattered over time and pattern setting industries do not exist (like in France and Belgium). A greater degree of synchronization is thus likely to shift the real wage curve downwards as shown in the Figure.

FIGURE 1



2.2.3 Workers' Militancy

Militancy is a (costly) response to workers' discontent; under normal circumstances, a reduction in the level of dissatisfaction will lead to a reduction in the level of activism. Militancy can be dampened by repression or by the imposition of economic costs such as the threat of unemployment. However, the use of political or economic costs as weapons to reduce labor militancy have long been (partially) replaced in industrialized countries by the introduction of social benefits that protect workers against market fluctuations. As the risk or costs to the worker of being unemployed are reduced, the incentives to mobilize and the levels of industrial conflicts tend to fall.

As noted by Esping-Andersen and Korpi (1985), social policies were introduced in European countries in two steps. First as an attempt by the ruling classes to preserve social stability (social reforms imposed "from above"), and then through the actions of unions and social democratic parties.[15] Therborn (1986), in the same vein, argues that in some industrialized

[15] Esping-Andersen and Korpi (1985, pp. 180-1):

countries an institutionalized commitment to full employment developed either as a result of "the concern of *certain bourgeoisies with social stability*," or as a result of "the wish of *strong labour movements for full employment* " (p. 111). Quite clearly, the propositions put forward by these authors imply that social reforms and the commitment to full employment were the outcome of a process of political struggle in which workers' militancy and organization played an important part. To the workers, unemployment benefits and the government's commitment to full employment programmes are two major shields against market fluctuations. To the ruling classes, they imply a redistribution of income in favor of workers in exchange for social order.

However misleading cross-country comparisons may be, it seems that a negative correlation can be identified between unemployment compensation and (commitment to full) employment[16] on the one hand, and labor militancy (as measured by strike activity) on the other hand. On Table 4, those countries where the rate of unemployment was relatively low in the early 1980s and unemployment benefits are higher are precisely those where the level of strike activity was lowest, namely, Austria, Japan, Norway, Sweden, and Switzerland. Canada, Australia, France, Italy, the UK, and the US are on the opposite pole of the spectrum. Denmark, the Netherlands, Finland, and Germany do not fit the generalization attempt.

In inflation-prone economies, wage policies are an important source of protection to workers' incomes. If wages are adjusted to inflation and the adjustment period is not too long, major wage reductions can be avoided. The protection of real wages against the acceleration of inflation and unemployment benefits plays a very similar role: they both insulate the income of workers from two variables (the price level and the rate of unemployment) that are out their control. In this sense, wage policies designed to protect wages against inflation also tend to reduce the level of workers' militancy. The inverse is also true, that is, when wage controls aim at the reduction of inflation through forced wage restraint (reductions in real wages) they tend to increase militancy and conflict. That is why in many recent stabilization attempts in Latin America, when the government tries to reduce inflation by deindexing wages or increasing the length of the indexation period, the level of conflict immediately increases.

> With only a few exceptions, the welfare states of Western nations developed up to 1945 as a result of social policy imposed "from above," where the working class was the *object* of the concerns and worries of the traditional ruling elites. As a result of improved capabilities for collective action during the first post-war decades manifested, for example, in significantly higher levels of unionization and leftist voting, the representatives of the working class increased their influence in legislatures and governments. This improved power position then enabled social democratic parties to become...the *subjects* of welfare state development.

[16] Therborn (1986) argues that the only countries where the level of unemployment was kept low in the late 1970s and early 1980s were those in which a commitment to full employment existed: Austria, Japan, Sweden, Norway, and Switzerland.

2.2.4 Trade Dependency and Policy Accommodation

Given the institutional setting on the basis of which wages are determined, there are other subsidiary factors usually seen as relevant in explaining wage restraint. One is the degree of trade dependency (B.2 on Table 1) and the other is the degree of policy accommodation of inflationary pressures which partly determines the actual levels of inflation and unemployment (given the "position" of the Phillips curve) and indeed influences the trade-off itself between the two variables.

TABLE 4

Commitment to Full Employment, Unemployment Benefits and Workers' Militancy

	Rate of Unemployment*	Unemployment Benefits**	Strike Activity#
Belgium	13.9	---	156
Canada	11.8	42.9	707
Denmark	10.6	86.0	148
Netherlands	13.7	---	22
UK	13.0	32.0	375
Average	10.0	53.6	283
Australia	9.9	---	427
Finland	6.1	42.0	358
France	8.4	42.9	278
Germany	8.0	67.4	28
Italy	9.8	17.4	849
USA	9.5	36.3	411
Average	11.5	41.2	391
Austria	4.1	---	10
Japan	2.6	68.9	71
Norway	3.3	59.0	28
Sweden	3.5	93.0	95
Switzerland	0.9	---	1
Average	8.1	76.6	41

* Percentage of labor force in 1983. Source: Therborn (1986).

** Percentage of average wage. Source: Therborn (1986).

\# Working days lost in industrial disputes per 1000 in total labor force. Source: ILO as reported by Cameron (1985).

Trade dependency—or the extent to which an economy depends on foreign trade—is both a matter of structural (given) constraint and (choice of) development strategy. In connection with the theme of wage determination, economic openness is important for it sets external limits to increases in prices, and thus affects the behavior of employers in wage bargains. A firm that exports 100% of its output is bound to set its price equal to the international level, and therefore is willing to restrict wage increases more than other firms that only sell in the domestic market and have their market shares protected against foreign competition. The former is the case of a significant proportion of the firms in small open economies such as the Scandinavian countries, Austria, the Netherlands, and Belgium. In comparing these economies with the large industrialized economies, Katzenstein (1981) notes that they:

> are unusually open to and dependent on a global economy which is beyond their control. The economic structure of the small European states is less diversified than that of the large states. Furthermore the small European states depend heavily on the import of investment goods and other products for which their small domestic markets simply do not offer large economies of scale. Instead they seek these economies of scale through a specialization in their exports (p. 101).

Katzenstein and others (Lange 1981 and Lloyd and Flanagan 1971 for example) have argued that there is an important relation stemming from trade dependency to corporatist structures and wage restraint. Since wage and price restraint are imperative in open economies, the incentives for cooperation between labor and capital (in some cases under the leadership of the government) are very large.[17]

To a certain extent, openness is also a question of choice. Indeed, the degree of trade liberalization is a strategic issue being debated in many countries today. Large economies can seek an autonomous route (like Brazil and India have done) but the advantages of such an option have been scrutinized in recent years under the argument that the lack of competition discourages the incentives for innovations and the search for productivity gains. It also has the perverse effect of reducing the limits of wage and price increases.

Policy accommodation is also an important factor in explaining the position of the curve depicted in Figure 1. Much as in the case of trade dependency, it is a question of choice but it has strong structural roots. In principle, the government can inhibit inflationary pressures by adopting a tight monetary and fiscal policy thus increasing the tension of the goods and labor markets constraints. However, the extent to which this is actually a choice is not very clear. Governments are in principle autonomous and may have an idea of the relation between policy instruments and

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[17] Referring to the small European economies, Katzenstein (1981, pp. 113-4) notes that they "have tried to restrain their wages and, occasionally, prices either through a government-coordinated incomes policy (as in the Netherlands and Denmark), or through a centralized system of collective bargaining (as in Sweden and Norway) or through a combination of the two (as in Austria)."

their outcomes. But in many circumstances, in face of certain compromises (most prominently when some kind of concertation is in place), or as a result of limits imposed by side effects of nonaccommodative policies, the government is incapable of pushing the brakes. Situations of political stalemates in which the government does not have the required support of major social agents to impose restrictive monetary policies abound in history.[18]

2.3 Stabilization Policies

In this section we discuss the prospects of three broadly defined varieties of stabilization policies in face of three different "social systems" where the latter are predominantly characterized by their industrial relations structures. The reduction of inflation is assumed to be the primary goal of the policies. We look at three systems—corporatist/hybrid I, pluralist, and hybrid II—and three stylized policies or "solutions"—market policies, concerted incomes policies, and non-negotiated incomes policies. We ask to what extent each of these policies is (ir)relevant, (in)feasible, and (in)effective, and what is the level of costs (as measured by increases in unemployment, poverty, and inequality) associated with each of them, in each of the three social scenarios. Table 5 summarizes the suggested outcomes.[19]

TABLE 5

Varieties of Stabilization Approaches in Alternative Social Scenarios

	Corporatism or Hybrid I	**Pluralism**	**Hybrid II**
Market solution	Relatively unimportant	Effective	Very costly
Concerted incomes policy	Effective	Infeasible	Infeasible
Non-negotiated incomes policy	Unrealistic	Ineffective	Ineffective

[18] As we suggest in Part II of the paper, such a situation of stalemate is probably the best characterization of what is happening in Brazil today, as well as in other Latin American countries like Argentina.
[19] A simple model illustrating the possible outcomes of alternative stabilization approaches under different institutional circumstances is developed in an appendix to the paper.

Governments use restrictive monetary and fiscal policies to reduce the market power of economic agents, and thus curb the creation of inflationary pressures. In order to successfully implement this kind of policy the government must be prepared to face the (political and electoral) losses stemming from the dissatisfaction of the losers—and there are many in the short run though not necessarily so many in the long run. The existence of safety nets (e.g., unemployment benefits) mitigates the costs associated with the policy. Depending on the extent to which agents' market powers depend on the conditions of the economy—a condition that ultimately hinges on structural and institutional factors—the required costs to segments of the society may be large or small. In pluralist systems this type of policy is usually feasible and efficacious and the social costs relatively small. The prospects of market solutions are thinner in situations in which there is a large number of powerful agents, such as in the case of hybrid II systems.[20] In these cases, agents are able to resist reductions in their standard of living, thus requiring a greater injection of market repression to respond to the policy. Hence the trade-off between inflation and unemployment tends to be greater.[21]

The conditions for concerted incomes policies can be seen in terms of three headings: institutional, political, and economic conditions. Institutionally, it has become quite an accepted idea that centralized union and employers' structures and centralized bargaining are very important. Tarantelli (1983, 1986, 1987) has argued quite convincingly that not only is the centralization of negotiations an important condition but also the level of synchronization of negotiations. As noted above, these two conditions do not mutually imply each other. In the case of the Nordic European counties and Austria both centralization and synchronization are present. But in the case of Japan, for example, the degree of centralization is not that high but wages are determined almost simultaneously and pattern setters play an important role.[22]

From the political point of view, the extent to which labor is represented in the political market and the degree of inclusion of labor in the state (both through political parties and the administration itself) are usually seen as important factors accounting for the feasibility and efficacy

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[20] The administrations of Reagan in the US and Thatcher in the UK are well known for applying this strategy. The success of the policy in terms of the trade-off between inflation and unemployment strongly suggests that the degree of pluralism may be an important factor. Indeed, the US is known for its pluralist features, whereas the UK has many of the traces of hybrid II systems.

[21] Some economists have noted that where there is a clear segmentation in the labor market between "insiders" (unionized senior employed workers) and "outsiders" (nonunionized young unemployed workers), and wage bargains take only the former group's interests into account, the trade-off becomes even more stringent. See Blanchard and Summers (1986).

[22] Tarantelli is probably the only economist who recognizes Japan as a corporatist case owing to the high levels of synchronization of wage bargains and informal centralized bargaining, and the importance of pattern setters. He notes that in Japan "bargaining takes place mainly at plant level, but it is heavily and yearly coordinated during the so-called spring offensive by all three major trade unions and the government. There is, in addition, a high degree of pattern bargaining" (1987, p. 97).

of negotiated incomes policy. Cameron (1985) notes that the presence of labor and social democratic parties in governments is an important element in explaining the relative success of some countries in dealing with the crisis. Regini (1985, p. 128) argues that militancy moderation is usually exchanged for unions' participation in policy-making:

> The state devolves portions of its decision-making authority to trade unions, by allowing them to play a part in policy formation and implementation and, thus, to gain advantage from the material and symbolic resources which the state can distribute. In return for this, trade unions deliver their indirect political power to the state by guaranteeing consensus and by drawing on their own resources to ensure the legitimacy, effectiveness and efficiency of state action.

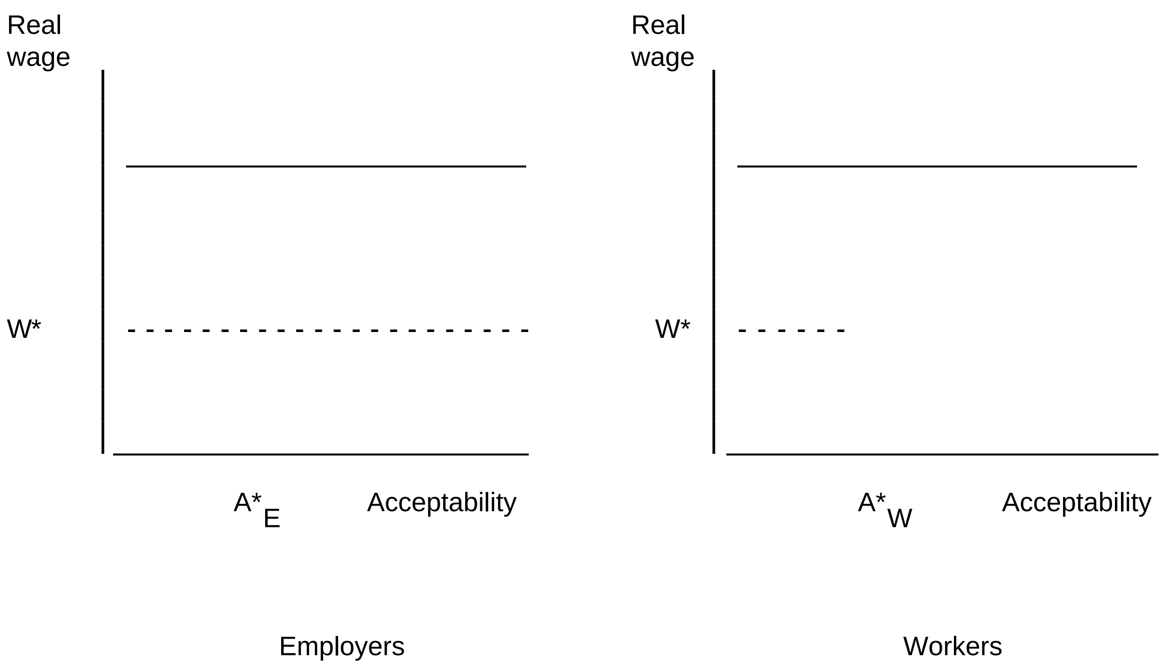
Where unions do not participate in the political market, and hence are not involved in political exchange, the best strategy is to explore to the limit their bargaining power in the economic arena. The result, depending again on structural and institutional factors, may be lack of wage moderation, on the one hand, and the infeasibility of concerted incomes policy, on the other.

Mutual credibility among the actors and legitimacy of the leadership (which imply compliance of the rank and file with the agreed policy) are yet other important factors accounting for the possibility and potential efficacy of concerted incomes policies. When the recent history is one in which one of the negotiating parties has not complied with the agreed terms of the policy (either for lack of legitimacy or other reasons), the other parties will be less inclined to participate in cooperative actions.

Finally, there are economic conditions. Here the important theme is the degree to which participating agents agree on certain goals, and the related distribution of costs. A central area around which a certain degree of consensus is critical is the distribution of income seen not only in respect to the conflict between wages and profits but also in reference to relative key prices and wages. Agents must agree on the distributive effects of the policy, and therefore the "degree of acceptability" of the agents attached to different distributive outcomes must be roughly consistent. Let us take the real wage as a representative distributive variable. In Figure 2, the panel on the left depicts the degree of acceptability of employers associated with different levels of the real wage. Ceteris paribus, employers may be prepared to accept increases in the real wage, but the degree of acceptability falls as the real wage increases. On the right panel, the workers' degree of acceptability is depicted. We have two cases to consider. If, for example, positive levels of acceptability of both employers and workers do not coincide (as in the case of curve A), the prospects of successful cooperation are nil. If, on the other hand, there is a range of wages to which positive degrees of acceptability of both employers and workers exist, the prospects become greater. Indeed, if a high degree of acceptability of both parties is associated to a certain level of the real wage, then an accord becomes possible.

In economies with high and accelerating inflation, it becomes very difficult to find a set of ranges of distributive variables to which reasonably high degrees of acceptability can be attached. Periods of inflationary surges are accompanied by large distributive fluctuations which in turn lead to episodes of distributive conflict. An attempt to establish a solution under such circumstances will find “winners” trying to preserve their current positions, and “losers” demanding significant changes in their positions. Hence the prospects of cooperation become very small.

FIGURE 2



Some special circumstances may create conditions for concertation. One is the existence of an external factor that poses significant limits to the well-being of all agents such as foreign competition. If recognized as a major element negatively affecting a majority of the agents, external threats can mitigate the force of conflicting interests, and favor cooperation. A situation of progressing crisis, which as a result of perverse negative feedback effects ultimately hurts the interests of all groups, can also engender cooperation. However, as in the case of the external threat, the incentives to cooperate will only materialize if the agents become conscious of their inability to cope with the crisis isolatedly, or more to the point, become conscious that the pay-off associated with the cooperative solution is greater than the pay-off associated with the exploration of individual market forces. A prisoner’s dilemma situation is likely to prevent cooperation. This is true especially in cases in which the number of players is large enough to inhibit negotiations, and their market power is sufficiently large to create the illusion that free-riding is preferable to the cooperative outcome.

Given these conditions, it seems obvious that concertation is inconceivable in pluralist systems and hopeless in hybrid II systems. In circumstances in which there is sufficient centralization of interests representation, but the political or economic conditions do not apply, concertation is also very difficult.

A last policy approach to stabilization is the adoption of a non-negotiated incomes policy which usually take the form of wage and price controls. That is, an attempt by the government to determine the “desired” levels of prices and wages, and thus distribution and relative prices. All the problems faced by concerted incomes policy plus some others are present here. To be successful, this approach requires that the government has either coercive or persuasive instruments to force or convince the agents to comply with the guidelines. Authoritarian regimes have the coercive powers. Legitimate and popular governments have some persuasive appeal. But the incentives to free-ride are always present and will tend to have undesirable consequences in the case where agents are relatively strong. Democratic governments can always use market instruments to force the agents to comply with the controls. But the bottom line is that the degree of difficulty becomes greater as we move from the pluralist to the hybrid II system.

We conclude by noting that there are policies that are more or less appropriate depending on the extent to which the economy is closer to the pluralist or corporatist pole. Some policy approaches are simply infeasible under certain circumstances; others are feasible but vary in the degree of efficacy and costs attached to them depending on the circumstances. Finally, it is worth noting that in hybrid II systems, market solutions are very costly, concerted policies are impossible, and non-negotiated incomes policies tend to have a low degree of efficacy. As a corollary we are led to conclude that if institutional designs are seen as a matter of social choice, intermediate cases should be avoided.

3. CONCLUDING NOTES

Economists, and more prominently policymakers, like to think that in face of certain problems (inflation or unemployment, for example), there exists a universally valid and correct set of policy prescriptions that, if appropriately implemented, would resolve the maladies of the economy. Indeed, many of the diagnoses and prescriptions offered by international agencies such as the IMF and the World Bank are in this vein. The government is somehow seen as omnipotent and able to choose the right policies, and if they do not pursue them, it is argued that some kind of perversion (corruption being a good example here) exists in the system. More sophisticated analyses of the Latin American cases attribute the causes of the mismanagement of the economy to “populism”—defined as the incapacity of the government to restrict its activities to its means and therefore accommodating inconsistent demands (see Sachs 1989 and Dornbush and Edwards 1989).

In fact, it is not true that there exists a universal set of policies to cure macroeconomic diseases. Different policies are more or less appropriate according to historical and institutional givens and conjuctural circumstances. Moreover, in face of certain constraints, some (or most or all) sets of policies may be prove to be undesirable, infeasible, or even worse, ineffective. In another paper, coauthored with Tariq Banuri (Amadeo and Banuri 1989), we argued that

> contrary to what is suggested by economists’ monistic vision...governments are neither all-powerful nor completely powerless in most areas of social activity. First, polities as well as governments are characterized by differentiation and tension, rather than by monolithicity of structure and function. In order to understand the functioning and consequences of social decision-making, it is important to replace monistic perspectives with more pluralistic views...and to see policy-making as the constrained decisions of one among many actors operating in a situation of conflict and tension, rather than autonomous actions of an independent and omnipotent actor (p. 3).

The case of populism, seen by some economists as a cultural aberration characteristic of Latin American social structures, can be seen as a response of weak governments in face of conflicting interests of private actors. The weakness of the government really implies that it would be difficult, if not impossible, to preserve some kind of political support without creating inconsistent forces at the macroeconomic level. In such cases, in place of adopting policies that would create the conditions for the achievement of certain goals under the restriction of some long-term constraints, the government maximizes its short-term political support at the cost of ultimately creating significant macroeconomic imbalances.

The case of exchange rate devaluations is paradigmatic in this respect. In face of balance of payment imbalances in the early 1980s many governments in Latin America promoted “maxi-devaluations” of the national currencies in order to induce changes in relative prices in favor of tradable sectors. Where actors (both firms and workers) in the nontradable sectors were able to resist the loss in their real incomes, the policy led to the acceleration of inflation, ultimately defeating the primary objective of the policy. In many cases, in order to coordinate the aimed at change in distribution, the government had to create deflationary pressures. In most cases, as in the case of Brazil, some degree of real devaluation of the currency was attained at the cost of greater unemployment and higher rates of inflation.

The arguments presented so far should not be interpreted as a nihilist manifesto. Certain sets of policies are more appropriate than others given the circumstances, and some may be quite successful. This is true in the case of many economies over considerable periods of time—the cases of the Nordic countries, West Germany, and Japan in the last three or four decades are quite obvious in this respect. However, the successful stories must be seen in terms of the underlying circumstances in which the policies were implemented.

Appendix: Stabilization Approaches under Different Social Structures

In Part I of the paper we have argued that different stabilization approaches may be more or less appropriate depending on certain institutional features of the social structure. The degrees of centralization and synchronization of wage bargains were taken as the central determinants of social structures. It was further argued that in some cases policies might be either infeasible or ineffective or else be associated with very high social costs. The model presented here is designed to illustrate the results put forward in the body of the text.

We focus our attention on the behavior of a representative union and a representative firm, thus abstracting from particular issues arising from decentralization of bargains. We assume that given certain factors (such as the degree of protection of the economy, the oligopolist power of firms, and the level of activity of the economy), the rates of change of money wages (w) and prices (p) arising from wage negotiations and the decisions of firms, respectively, would be given by the following equations:

A.1 $$w_t = j\, p_{-1}$$

A.2 $$p_t = e\, w_t$$

where j is the indexation parameter of wages to past inflation and e is the indexation parameter of prices to wage costs. These two equations together imply a relation between the rates of inflation in periods t-1 and t:

A.3 $$p_t = j.e\, p_{-1}$$

Note that there is an infinite number of combinations of parameters j and e consistent with the ratio $p_t / p_{-1} = k'$:

A.4 $$j.e = k'$$

Let us now assume that the government sets a target rate of inflation for period $t(p_t{}^*)$. Given $p_t{}^*$, a new function relating j and e to the rate of acceleration of inflation $p^*{}_t / p_{-1} = k^*$ arises:

A.5 $$je = k^*$$

Equations A.4 and A.5 are depicted in Figure A.1. For k* < k’, the k* curve must be associated with lower values of j given e (or e given j) compared with the k’ curve. Therefore, if the k* rate of acceleration of inflation is to be effective, the values of parameters e and j will have to accommodate to the policy target.

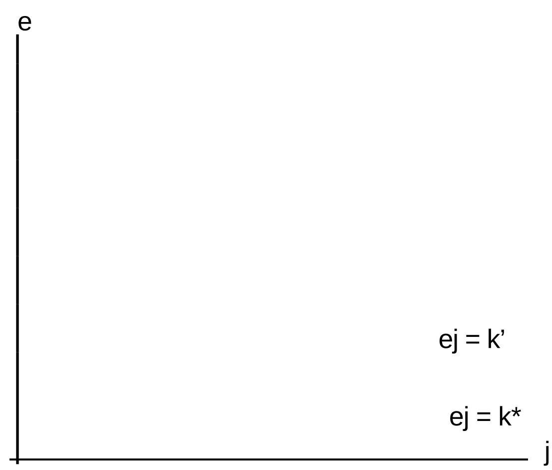


Figure A.1

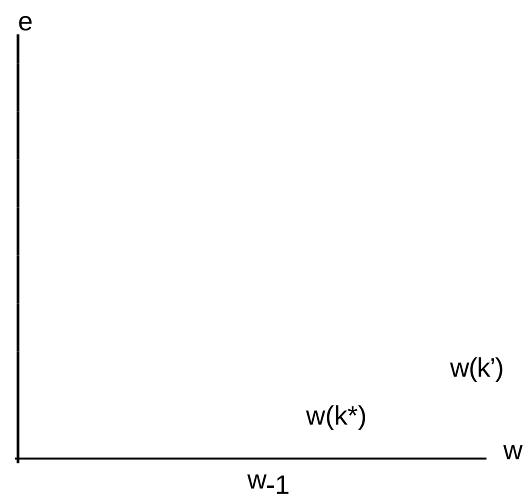


Figure A.2

We take the real wage as a measure of the distribution of income, and note that, in face of the above equations, the real wage will depend on the values of parameters j and e, on the one hand, and the rate of acceleration of inflation, on the other. Given the value of k, the relation between the real wage (W), and parameters e and j will be given by:

A.6 $$W = W\{[1 + jp_{-1}] / [1 + jep_{-1}]\} = W\{[1 + (k'/e)p_{-1}] / [1 + kp_{-1}]\}$$

The relations between the indexation parameter of prices, e, and the real wage associated with k' and k* are depicted in Figure A.2. Note that for e > 1, the real wage will fall in relation to the real wage in the last period, and vice-versa, no matter what the value of parameter j happens to be. A change in k implies a rotation of the curve around the (W, 1) point.

In order to take into account the role of market forces in the determination of wages and prices, we assume that both parameters j and e are functions of the rate of unemployment:

A.7 $j = j(u)$ and $e = e(u)$ with j' and $e' < 0$

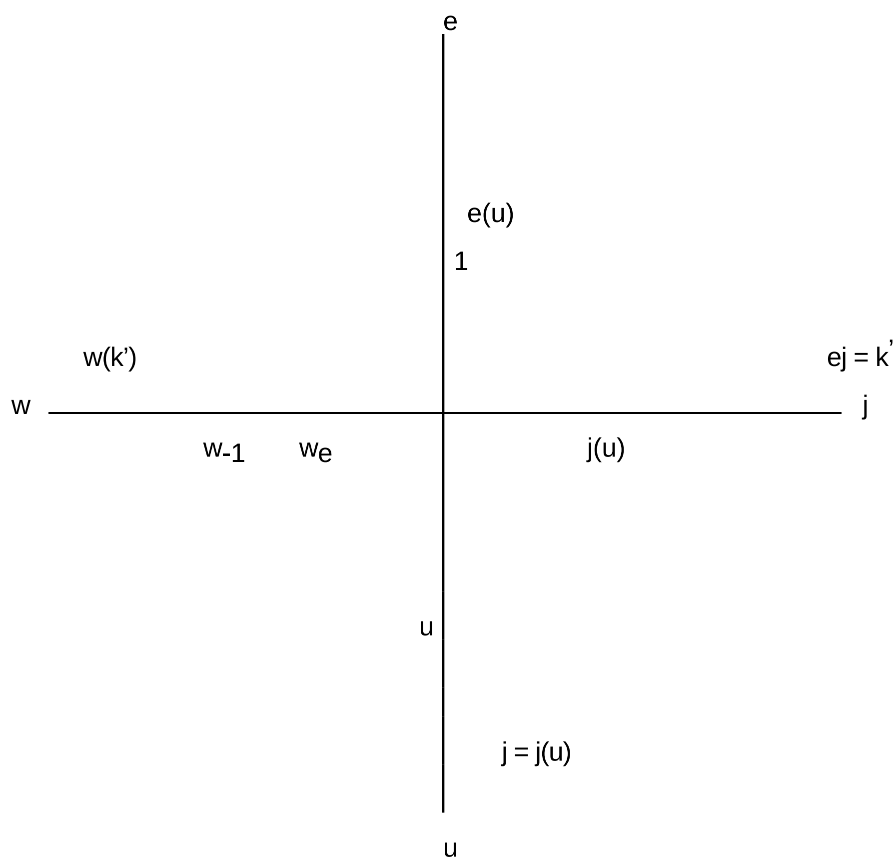


Figure A.3

given the rate of unemployment, which we assume is under the control of the government, and the relative bargaining power of the union and the firm, the indexation factors j and e are determined, and also the real wage. Figure A.3 depicts the equilibrium configuration.

1. Market Solution

Let us assume that the government has control over the rate of unemployment, that is, that by altering its monetary and fiscal policy it can determine the rate of unemployment. In order to force the system to converge to $k = k^*$, the government can increase u up until the point at which $j.e = k^*$. The way parameters j and e will change to accommodate the target rate of inflation will depend on the sensitivity of each with respect to changes in the rate of unemployment. Indeed,

$$(dj / du)\, e + (de / du)\, j = dk < 0$$

so that

$$E(j,u) + E(e,u) = (dk / du)\, u < 0$$

where E(...,u) is the elasticity of j (or e) with respect to changes in the rate of unemployment. These elasticities depend on the bargaining powers of unions and firms. The new equilibrium configuration is depicted in figure A.4.

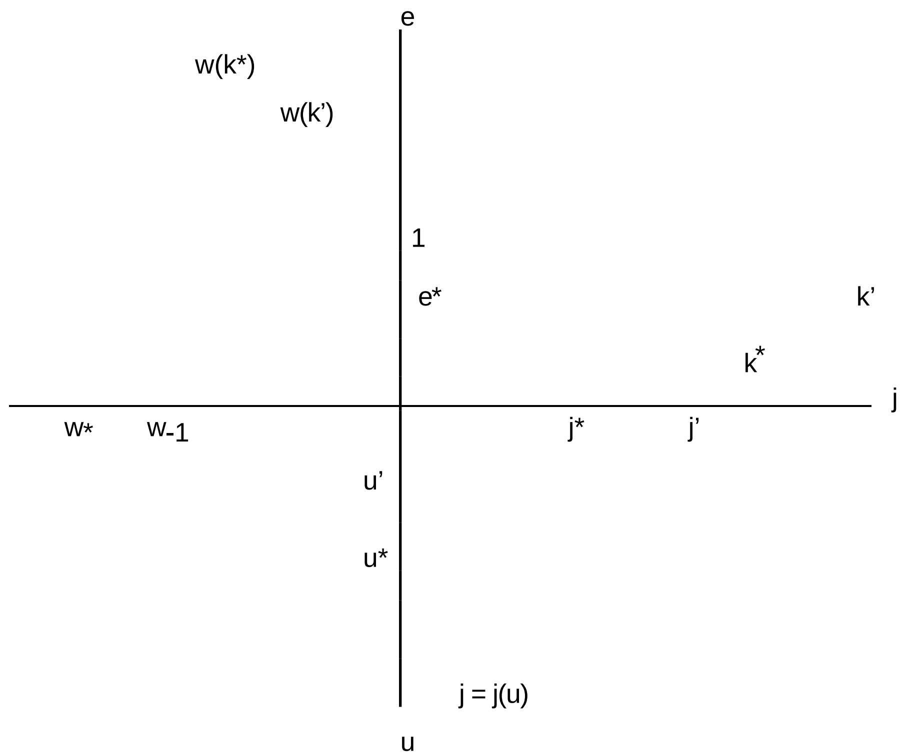


Figure A.4

The rate of unemployment is higher but the real wage is not necessarily higher or smaller than before. If we assume that firms maximize profits and equate marginal revenue to marginal costs, then the higher level of unemployment ought to be associated with a higher real wage. If we allow some kind of market imperfection, in principle the real wage can either be greater or smaller than before. The important thing to note is that the market solution will have effects on the rate of unemployment and the distribution of income. In pluralist structures the increase in unemployment required to bring down inflation is smaller than in hybrid II structures in which the elasticity of both parameters j and e with respect to unemployment are supposed to be smaller.

2. Concerted Incomes Policy

Let us assume, for the sake of the argument, that the government's diagnosis is that (i) the acceleration of inflation is due to over-indexation of wages, that is, $j(u) > 1$; and that (ii) prices are under-indexed with respect to changes in wages so that $e(u) < 1$. Hence, the rate of acceleration of inflation is given by $k' = j.e > 1$, and real wages are growing over time. The government could attempt to stabilize the rate of inflation (make $k^* = 1$) by convincing the workers' representatives that instead of promoting a deflationary policy, stability could be attained if workers were to accept the just-indexation of wages to inflation. The stabilization of real wages over time (with $j = e = 1$) would imply a stable rate of inflation, and in principle is consistent with the same rate of unemployment, or even a lower rate of unemployment. If the union values employment conservation, it would have an incentive to accept the government's proposal. In this case the union would be under-exploiting its market power in exchange for a job security agreement. Figure A.5 depicts the adjustment.

If the firms are over-indexing prices, no matter what the degree of indexation of wages is, real wages would be falling over time. Here the situation is more difficult since the government cannot ask for wage moderation if firms do not agree to reduce the level of price indexation. In this case, the government could threaten firms with greater taxation, or convince them to reduce the level of indexation in exchange for a lower degree of industrial conflict and instability and smaller government deficits which, in the long term, could benefit the firms. Depending on the extent to which firms can see the damaging effects of inflation in the medium and long runs, they will or will not be sensitive to the government's appeal.

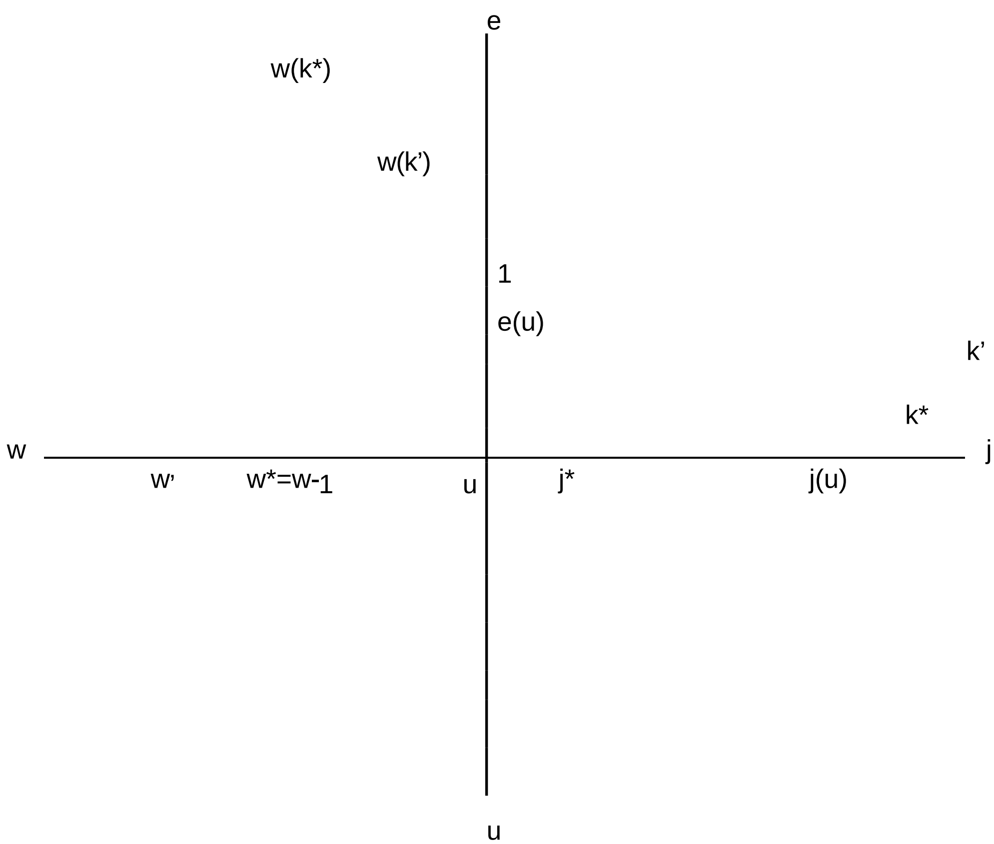


Figure A.5

3. Non-Negotiated Incomes Policies

In non-negotiated incomes policies, the government sets the degrees of indexation of wages and prices, say j = e = 1. If the government is not able to convince the agents that there are benefits stemming from stability to be shared between workers and firms, and if it does not use for lack of political support, or does not have the power to use, coercive instruments, there will be strong pressures for a return to the status-quo-ante situation. The arrows in Figure A.6 indicate the direction of these forces. As far as market forces are concerned, the size of the pressures to over-index will be directly related to the gap between the required rate of unemployment to force j.e = 1, and the actual rate of unemployment.

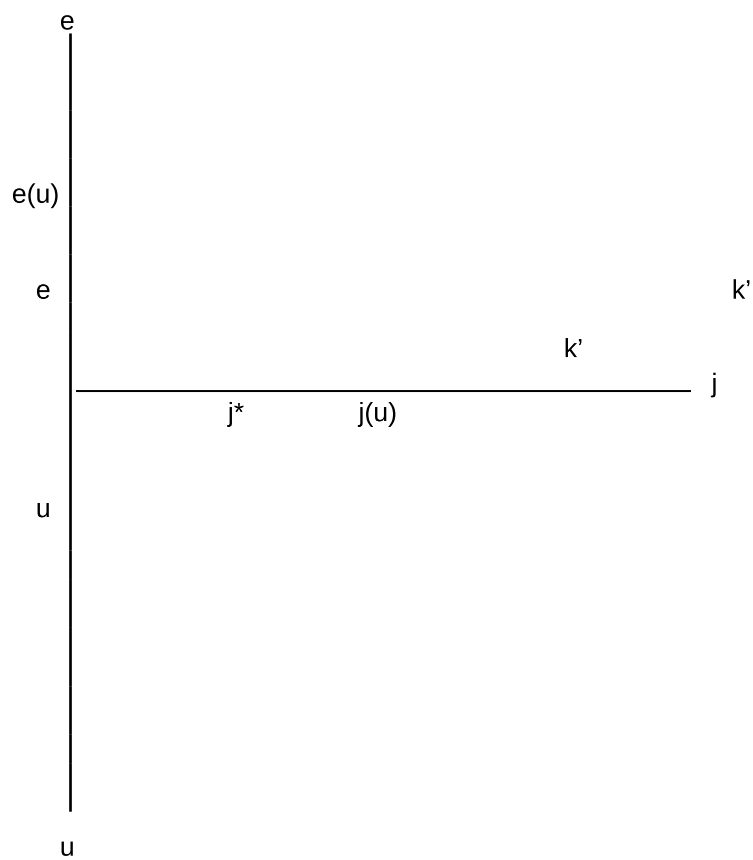


Figure A.6

The government can use market solutions to enhance the conditions for wage and price restraint, but the same problems associated with the market approach would be present here as well.

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