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European Unemployment:
Macroeconomic Aspects

Europe as an Entity,
Possibilities and Limits
in Economic Policy

HENRIK HOFMAN

RSC No. 97/49

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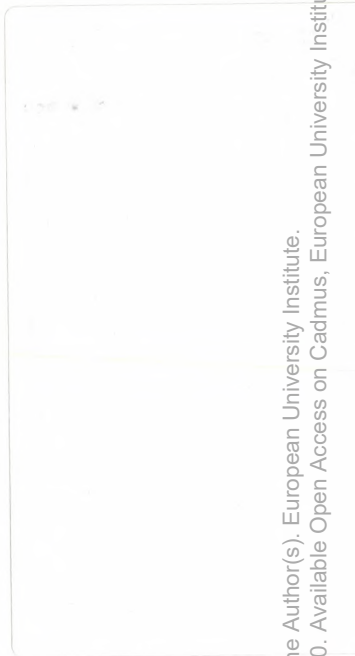
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ROBERT SCHUMAN CENTRE

**European Unemployment: Macroeconomic Aspects
Europe as an Entity.
Possibilities and Limits in Economic Policy**

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European Unemployment: Macroeconomic Aspects
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In the latest Annual Report The European Monetary Institute says that "the high level of unemployment, standing at almost 11% for the EU as a whole at the end of 1995, primarily reflects structural problems". In the report it is also said that the main challenge for EU is fiscal consolidation and that fiscal consolidation does not necessarily lead to contractionary effects even in the short run. The third major point in the report is the recommendation that monetary policies should be geared towards the primary objective of price stability.

Probably only a very few economists would today argue against the goal of achieving low inflation and sound public finances, nor will I. But I will in the paper show that it is very important that the economic analysis of the development in EU and Europe is not done in a "bookkeeper-way". By this I mean that it is very important to analyse the possibilities and limits in economic policy not only from a national point of view but also from an European level.

I find that some of the recommendations to the economic policy in Europe in The European Monetary Institute's Annual Report are quite problematic. The basic reason for this is that I find that these recommendations are mostly given to the European countries as individual and independent countries. The importance of the economic interaction between the European countries is in that way devaluated.

In the paper¹ I will try to show why it is very important to analyse the possibilities the economic policy from an European level and not from a starting point where 15 individual countries are compared.

An European National Account

Following one of the longest recessions in the post-war era the European economy is now slowly recovering.

To understand both the recession and the upswing in Europe, it is important to have adequate information of the factors that determine the European growth and employment. A first step to this understanding is to get information about the European GDP and it's components examined as a hole, i.e. an European National Account. Instead of looking at Europe from the national point of view - which is often seen - we will look at Europe as one economy.

¹In writing the paper I have benefited from many valuable comments from my colleagues Lars Andersen and Thomas V. Pedersen

Growth rates in Europe fell in the beginning of the 1990'ies. In 1993 the growth rate became even negative. Output expanded again in 1994 and 1995 but this expansion came quite quickly to a marked slowdown again in 1996.

The main reason behind the recession in the beginning of the 1990'ies is to be found in the development of domestic demand. It is not foreign trade which has worsened the employment situation. Net-exports gave in 1993 a significant positive contribution to growth in GDP.

In 1988 the GDP growth rate was 4.0 per cent in Europe. Four years later in 1992 output growth was reduced to 1.0 percent and became negative in 1993. The main reason behind the lower growth rates was a fall in the contribution to output growth from final domestic demand from 4.2 per cent points in 1988 to -1.2 per cent points in 1993, cf. table 1.

Table 1. Contributions to changes in real GDP growth in Europe. Per cent points "

| | 1988 | 1990 | 1992 | 1993 | 1994 | 1995 | 1996 |
|-------------------------------|------|------|------|------|------|------|------|
| Gross domestic product | 4,0 | 2,9 | 1,0 | -0,6 | 2,8 | 2,4 | 1,4 |
| of this: | | | | | | | |
| Final domestic demand | 4,2 | 2,7 | 1,1 | -1,2 | 1,6 | 1,9 | 1,5 |
| Stock building | 0,3 | -0,1 | -0,2 | -0,4 | 0,9 | 0,2 | -0,3 |
| Net exports | -0,5 | 0,3 | 0,1 | 1,1 | 0,3 | 0,3 | 0,1 |

Source: OECD and ECLM

As shown in table 1, in 1993 the contribution from foreign trade was quite significant, 1.1 per cent point, which reduced the size of the downturn in 1993. There has also been a positive contribution to growth from foreign trade in 1994 and 1995.

It was certainly not foreign trade which caused the slow growth performance in the beginning of the 1990'ies. It was a totally "home made" recession.

Especially private consumption and total fixed investment have damped economic activity, cf. table 2. Private consumption and total fixed investment in 1988 gave a large positive contribution to real GDP changes on respective 2.2 and 1.6 per cent points. In 1993 there was no contribution from private consumption to output growth and the contribution from investment was considerable negative.

Table 2. Contributions to changes in final domestic demand in Europe. Per cent points

| | 1988 | 1990 | 1992 | 1993 | 1994 | 1995 | 1996 |
|------------------------------|------|------|------|------|------|------|------|
| Final domestic demand | 4,2 | 2,7 | 1,1 | -1,2 | 1,6 | 1,9 | 1,5 |
| of this: | | | | | | | |
| Private consumption | 2,2 | 1,6 | 0,9 | -0,1 | 1,0 | 1,1 | 1,0 |
| Public consumption | 0,4 | 0,4 | 0,4 | 0,2 | 0,2 | 0,2 | 0,2 |
| Total fixed investment | 1,6 | 0,7 | -0,2 | -1,3 | 0,5 | 0,7 | 0,3 |

Source: OECD and ECLM

Large Economic Interaction between the European Countries

To illustrate the great importance of Europe's domestic demand and the minor importance in general from foreign trade, table 3 shows the share of different components of GDP in Europe. Private consumption and fixed investments taken together make a total of about 80 percent of GDP, cf. table 3.

Table 3. Component's share of Gross Domestic Product, Europe.

Average of 1992-1996. Per cent of GDP

| | Imports | Private consumption | Government consumption | Total fixed investments | Exports |
|--------------------------------|---------|---------------------|------------------------|-------------------------|---------|
| Including intra-regional trade | 26,4 | 60,0 | 18,8 | 19,8 | 27,7 |
| Excluding intra-regional trade | 8,1 | 60,0 | 18,8 | 19,8 | 8,6 |

Source: ECLM and WTO

When one analyses the contribution from trade to economic activity it is important whether the contribution from trade includes or excludes intra-regional trade. Intra-regional import and export are trade from one European country to another European country. Since the major part of foreign trade in Europe is trade from one European country to another European country, the share of imports and exports excluding these intra-regional movements gives much smaller figures.

Therefore, one has to be careful not to exaggerate the challenges from these countries outside Europe for Europe's growth and employment situation. It is e.g. an exaggeration to state that further imports from Central- and Eastern Europe and the former USSR will significantly undermine the growth and employment

possibilities for Western Europe. Firstly, because total imports today from these countries are very small, and secondly, because Western Europe has exports of at least the same dimensions to these countries.

As to the employment level in Europe it is to be underlined that it is extremely important how the European countries cooperate. To get a sustained growth and a major improvement in employment we have to focus on the domestic demand in Europe. Higher exports to the rest of the world have improved the outlook for the European economy but to ensure a strong growth and a better employment situation we can not rely very much on foreign demand. This point is illustrated further in ECLM (1995).

The economic interaction in Europe implies that the economic activity in every single country has considerable effect on the other European countries. In table 4 it is tried to show these economic interactions for a chosen number of European countries. The table is made in such a way that for each country in the upper part of the table there is made a calculation where the economic activity in the concerned country is increased with 1 per cent of GDP by means of an increase in the demand in the private sector. In every column it is possible to see the effect on GDP of this in the other European countries.

Column 1 shows that an increase in the GDP level in Germany on 1 per cent through direct, indirect and derived effects will increase GDP in France with 0,21 per cent, 0,32 per cent in Italy and 0,14 per cent in United Kingdom.

Table 4. Increased economic activity. Effects on other European countries in the third year. Per cent of GDP

| | Germany | France | Italy | UK |
|-------------------|---------|--------|-------|------|
| Effect on GDP in: | | | | |
| Germany | 1 | 0,12 | 0,12 | 0,11 |
| France | 0,21 | 1 | 0,09 | 0,07 |
| Italy | 0,32 | 0,15 | 1 | 0,11 |
| UK | 0,14 | 0,05 | 0,04 | 1 |

Note: Deviations from baseline. The increased economic activity is created by private consumption.

Source: ECLM, simulations on HEIMDAL ²⁾

An increase in the French GDP on 1 per cent will increase GDP in Germany with 0.12 per cent. Column three and four show that changes in the economic activity in Italy and in United Kingdom have an equal large influence on the GDP level in Germany.

Politically, the ties are perhaps stronger between Germany and France than between Germany and United Kingdom/Italy. From an economic point of view there are, however, no major differences ²

Another way to illustrate the large economic integration between the largest European countries is to have a look at the effects of changes in the exchange rates. In table 5 is shown a simulation where the Italian Lira and the English Pound are both devaluated with 10 per cent against the other European currencies. With Germany and France as examples it can be seen that the counterpart to the gains in the employment in the short term in Italy and United Kingdom is a loss in employment in Germany and France.

Table 5. A devaluation on 10 per cent in Italy and UK in 1996. Effect on employment in year 2000

| Italy and United Kingdom | Germany and France |
|---------------------------|--------------------|
| ----- 1.000 persons ----- | |
| 480 | -260 |

Note: Unchanged real interest rates
Source: ECLM, simulations on HEIMDAL

The intention with the table is not only to show the exact numbers but, with the European perspective in mind, also to show the fact that changes in the exchange rates can not be used in an offensive manner to create more jobs in Europe. What we will see is mere a redistribution of jobs.

Much the same can be said to other kind of traditional competitiveness policies. We know that the majority of trade in Europe is between European countries, so policies like e.g. a general reduction in the European wage levels will only have minor effects on the total number of working places in Europe.

²So from an economic point of view even Germany should have a major interest in establishing a cooperation with countries which probably will not take part in the EMU from the start, i.e. establishing an EMS-II.

What is more important in a quite closed economy like Europe regarding the development in the numbers of working places is the general development in internal demand. This brings the European fiscal- and monetary policies in focus.

Effect of Economic Policy in Europe

The fact that Europe in an economic sense is an entity makes it important that the European countries cooperate and coordinate their economic policy. But when the objectives are to get a higher employment and a reduction in the enormous unemployment it is of course not unimportant how this cooperation is carried out.

The economic recession in the beginning of the 1990'ies differed from the former two great recessions of the post-war era, not only in nature but also in the effect on the employment situation. The previous two great recessions in 1974-75 and in 1980-82 respectively were supply shocks which were released by the drastic aggravation of the terms of trade in connection with the heavy oil-price increases. Total employment fell with approximately 2 million persons in the wake of each of the two supply shocks.

In the downturn to the trough in 1993 employment in Europe has been reduced with 5.5 million persons. It was much more than the number of lost jobs in the two former supply shocks put together. And employment has only increased very slowly in 1994-96.

The background for the recession of the European domestic demand after the 1980'ies boom ended was mainly a considerable private accumulation of debt during the mid-1980'ies boom.³

In particular three factors gave rise to the accumulation of debt. First, liberalizations of capital markets resulted in an increased supply of credit facilities - and often of a very risk prone nature. Second, a very slow adaptation to lower inflation meant that the size of the real interest and accordingly the loan-burden was underestimated. And third, a wrong monetary policy gave rise to accumulation of private debt.

Monetary policy by focusing on the development in commodity prices - e.g. on overall inflation - was directed towards lowering interest, as the tumbling down of energy prices was transformed into a lower general inflation. The combination of

For a survey see "Out of the Crisis - Economic Progress through International Co-operation", The Economic Council of the Danish Labour Movement, 1993.

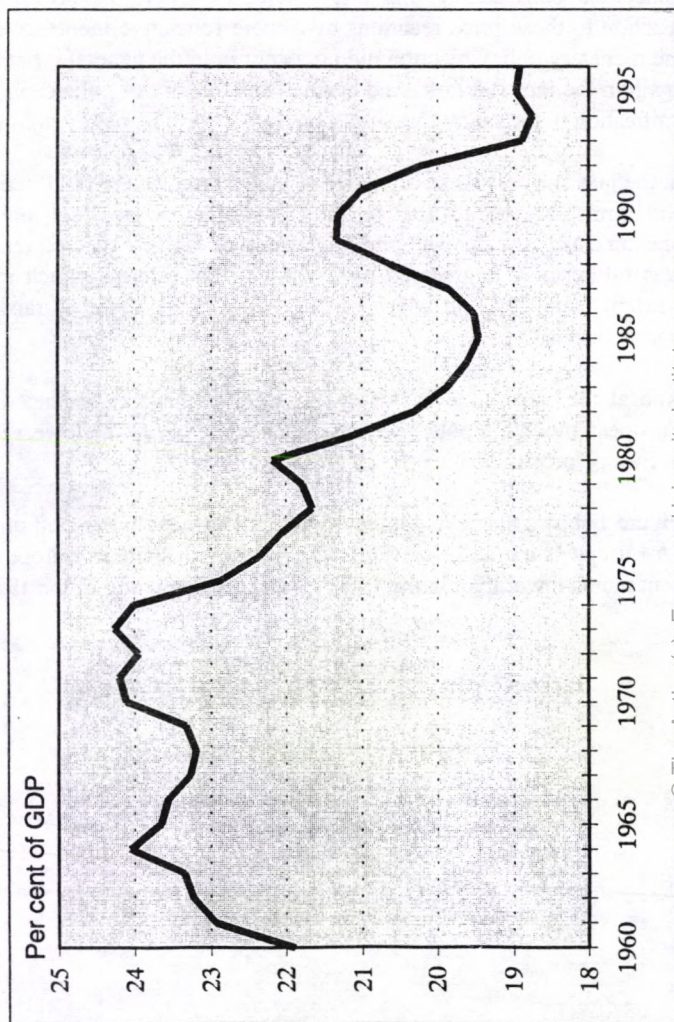
increased supply of loans and lower interest rates implied considerable increases in prices of real estate as well as heavily increasing share prices. Capital goods underwent consequently big price increases. There should have been a quick reaction to these price reactions by a more restrictive monetary policy. In stead, the monetary policy reaction did not occur until the general inflation began to rise again in the late 1980'ies. And besides this the mix of policies in the wake of the unification in Germany further put pressure on the monetary policy.

In the late 1980'ies these increases in interest rates were reinforced as households and firms started to realize that low-inflation was not only a temporary phenomenon. The demand pressing effects of higher expected real rate of interest was furthermore augmented by a wave of tax reforms which swept over most western countries, and which among other things aimed at raising the after-tax rate of interest.

And at the same time as we in the 1990'ies have experienced a much tighter European monetary policy we have been witnesses to the lowest investment share in Europe probably since the second world war.

Figure 1 shows the development in total investment in per cent of GDP calculated for Europe as a whole since 1960. The investment share in Europe is today 4-5 per cent points lower than in the 1960'ies and the beginning of the 1970'ies.

Figure 1. Total investment in per cent of GDP, Europe 1960–96



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We have also calculated the investment shares separately for business investment, investment in housing and government investment. These calculations show that each investment share has contributed to the general fall. The business investment share is 2 per cent point lower in 1996 than in the beginning of the 1970'ies. In per cent of GDP the government and the housing investment share is each approximately 1.5 per cent point lower in 1996 compared with the beginning of the 1970'ies.

This low level of investment in Europe will naturally have important influence on the future creation of working places and employment.

In a recently published analytical study from the EU-Commission they underlined the seriousness of this by saying that "The recession and the strong fall in fixed capital formation to less than 19% of the Community's GDP has indeed reduced the potential rate of growth to about 2 1/4 to 2 1/2 %, i.e. to a rate barely able to maintain unemployment constant." (The European Commission, 1996).

A conclusion in a growth and employment study will therefore be that in order to reduce unemployment it is absolutely necessary that Europe in the coming years strongly increases its investment share.

But in order to do so for the entire Europe it is important that such a task is done in cooperation and not only by a few countries because of the major economic interaction in Europe. We have the traditional free-rider problem, i.e. it can be difficult for one or a few countries to pursue such a policy because of derived deteriorations on the current account and also on the public budgets.

In table 6 we have made a simulation which can illustrate this dilemma. We have made two sets of simulations where public investment is increased with 1 per cent of GDP. In the first simulation it is only Germany which increase their investment share. In the second simulation it is all European countries which increase their investment share. In both calculations we illustrate only the effects of such a higher investment share on figures for Germany.

Table 6. An increase in public investments on 1 per cent of GDP from 1996. Effect in year 2000

| Effect on Germany | | | |
|---------------------------|--|--|--|
| | Only Germany raise the investment share | Every country raise investment share | European raise the effect on Germany |
| -----Per cent----- | | | |
| GDP | 0,7 | 1,2 | +0,5 |
| -----Per cent of GDP----- | | | |
| Government budgets | -0,6 | -0,4 | +0,2 |
| current account | -0,5 | -0,2 | +0,3 |
| -----Per cent----- | | | |
| Employment | +1,1 | +1,5 | +0,4 |

Note: In all calculations is it assumed that short term real interest rates are held constant

Source: ECLM, simulations on HEIMDAL

With Germany as an example of the importance of coordination of the economic policy, we can see that there is significant differences between the single country effort and the multi country effort.

The German GDP effect will be larger when more countries cooperate and there will be less negative effects on the public budget and the current account. Finally, we will also get a significant higher effect on German employment.

Because Europe is an entity it is therefore important that the European countries coordinate and cooperate. But when such a cooperation is decided it is also necessary to look into how the mix is made between the different policy opportunities. Especially it is of major importance how the mix is made between the fiscal and the monetary policy.

The mix between Fiscal and Monetary Policy

The importance of how fiscal and monetary policies are mixed is illustrated by calculating the effects of fiscal tightens in some of the countries which according to the Maastricht convergence criteria have to make fiscal tightens to reach a figure of maximum -3 per cent of GDP on the public budgets in 1997.

For Germany there is made a tightening which corresponds to a permanent fiscal retrenchment on 1.35 per cent of GDP. The tightening in France corresponds to a permanent retrenchment on 1.8 per cent of GDP. For Italy and Spain it is assumed that the fiscal tightening will only correspond to a fiscal retrenchment on 1.5 per cent of GDP, so they will not reach the Maastricht criteria in a short term. The effects on Europe is shown in table 7.

The table shows that the magnitude of the short term negative effects from fiscal tightens in several major European countries will depend very much on how the monetary policy is carried out.

Table 7. Effect on Europe in 1999 from a fiscal tightening in Germany, France, Italy and Spain in 1997.

| | Effect on Europe | | | | | |
|---------------------------------------|-----------------------------------|---------------------------|--------------------------------|--------------------------------|---------------------|-------|
| | Unchanged term nominal rate | short term interest | Unchanged term real rate | short term interest rate | Unchanged supply | money |
| Change in short term interest rate | 0 | -----Per cent point----- | | -0,23 | -0,42 | |
| | | -----Per cent----- | | | | |
| European GDP | -0,9 | | -0,7 | | -0,3 | |
| | | -----Per cent of GDP----- | | | | |
| European Government budgets | +0,5 | | +0,7 | | +0,9 | |
| | | ----- 1000 persons----- | | | | |
| European Employment | -1100 | | -875 | | -450 | |

Source: ECLM (1996)

If the monetary policy is tight when several countries implement fiscal tightening the negative effect on GDP and employment will be largest, cf. column 1. On the other hand if we have a monetary policy which also is targeted against employment and economic growth the isolated negative effects of fiscal tightens could be much lesser, cf. column 3.

It is then to be emphasized that the monetary policy should be allowed to operate with more flexibility and not only have price stability as its major goal.

Monetary Policy

Price stability is important but it should not only be achieved through a tight monetary policy. If this is done we risk major derived negative effects on the real economy and especially on the above mentioned investment share.

If we look upon the contribution to growth in Europe from fixed capital formation and compare that to a measure for the degree of monetary tightens in Europe it is possible to find some connections.

In table 8 we have calculated the average contribution to growth in Europe coming from investments. We have divided these contributions up on four business cycles in Europe. For the four business cycles we have further shown a measure for the tightens of monetary policy, namely a yield curve with the short term interest rate in Germany in per cent of the long term interest rate.

Table 8. Contribution to growth in Europe from investments and monetary tightens in Germany 1961-95

| | 1961-73 | 1974-85 | 1986-90 | 1991-95 |
|--|---------|---------|---------|---------|
| Average contribution to growth in Europe from fixed investment, <u>per cent points</u> | 1,3 | -0,0 | 1,1 | 0,1 |
| Short term interest in <u>percent</u> of long term interest rate (Germany) | 78 | 81 | 80 | 97 |

Source: OECD-databank and ECLM

It is very obvious from the table that the monetary policy was tightened in the period from 1991-95. A period in which there was almost no contribution to growth in Europe from investment.

We have the same poor development in the contributions from investment in the period from 1974-85. But the periods 1974-85 and 1991-95 were very different. In the period 1974-85 Europe was exposed to two major supply chocks. In the period 1991-95 Europe's terms of trade was improved. The chock here was an internal demand chock, partly caused by a tight monetary policy.

A Contribution to make Monetary Policy more Flexible in Europe

Better functioning of the labour markets is one of the major keys to take some of the pressure of monetary policy to keep inflation down. Therefore inflation problems have to be solved on the markets where they occur, i.e. on the good markets and on the labour markets.

This is why investment in labour - education and labour market policies - is an efficient policy in regard to have both more growth and higher investments without an inflation pressure. Improved flexibility of labour can prevent bottlenecks and thereby dampen the inflation pressure.

A higher level of education in the EU can also reduce our dependence of low technology productions, and thereby make it easier for third countries to enter the EU market. This will help to dampen inflation, and it will help the East and the South of Europe to increase their wealth.

Even though investment in education does not create a large amount of jobs in the short run, the educational effort will, even in the short run, bring about a large fall in the unemployment due to the replacement of people going on education. But the major effort which has to be done to improve the functioning of the labour markets in Europe is in a much lesser degree a matter which demands that Europe does the same things at the same time. The efforts both to increase the investment in human capital and to implement an up qualification strategy for the labour market are a task which primarily has to be done on a national basis.

One of the reasons why the effort to improve the flexibility of the labour markets has to be done on a national basis is that we can see, that the European labour markets are quite different. We do not have what one could call a homogeneous European labour market. Each country has its special characteristics. The structural differences in the European labour markets make it difficult to prescribe

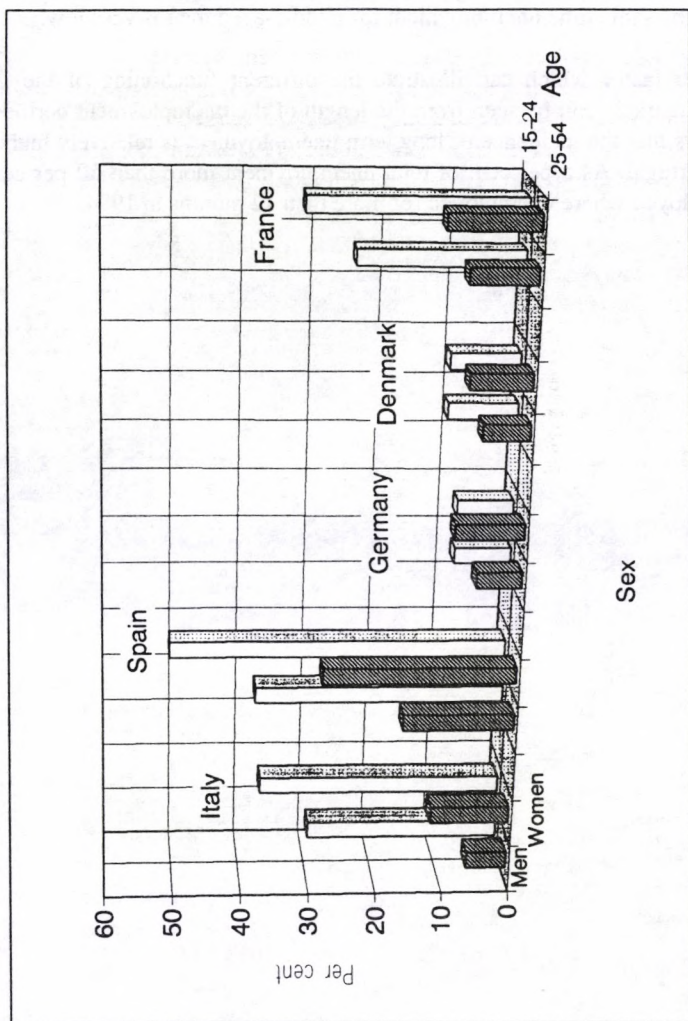
the same medicine. Especially on the micro level is it important that the policies fit into the culture in each countries.

Some of the differences arise because of different "cultures" about working time and part time work. In the Southern European countries the share of part time work is e.g. relatively low. Spain, Portugal, Greece and Italy have a low share of part time work, while it is more common in the Northern European countries, especially in The Netherlands, United Kingdom, Sweden and Denmark.

This difference in the organization of the European labour markets makes it difficult to recommend common major changes. Another obstacles to a general European labour market policy is that unemployment is unequal composed in the different European countries.

Countries like Italy and Spain have a very unequal composition of unemployment. In general unemployment is higher for women than for men, and unemployment in these countries is also considerable higher for the youth than for the middle aged workers. Also in France there are major differences in the risk of getting unemployed depending on whether the worker is a woman or a man and depending on the age, cf. figure 2.

Figure 2: Unemployment rates by sex and age, 1994

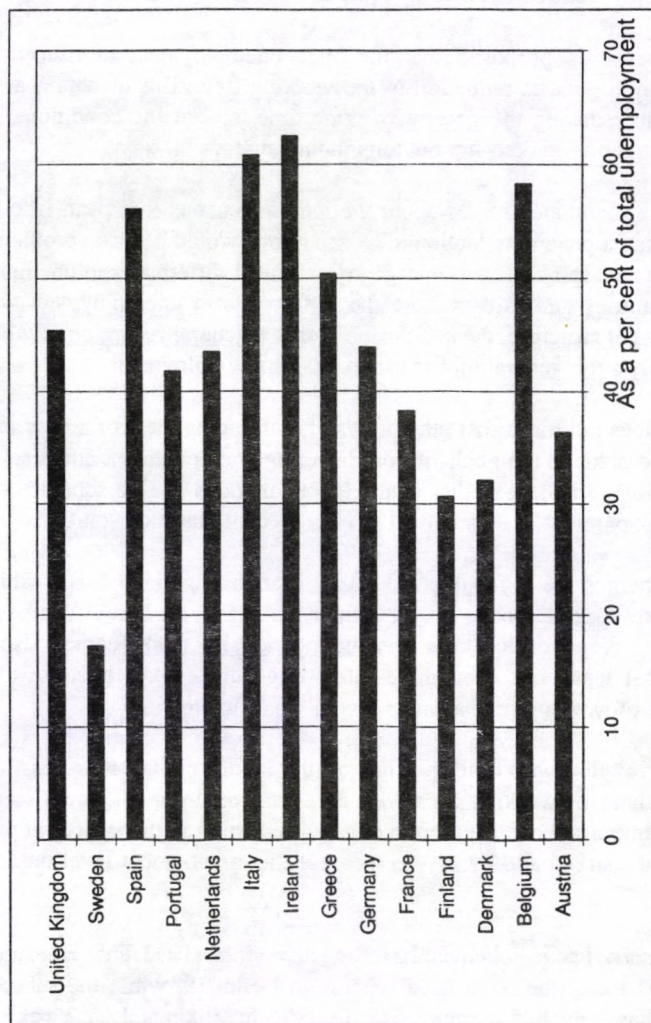


Source: OECD, Employment Outlook

In Italy unemployment is very high for the youth - especially for young women - and at the same time unemployment for middle-aged men is very low.

Another factor which can illustrate the different functioning of the European labour markets can be seen from the length of the unemployment periods. Figure 3 shows that the incidence of long term unemployment is relatively high in Spain and Portugal. As a per cent of total unemployment more than 50 per cent of the unemployed were unemployed for more than 12 months in 1994.

Figure 3: Incidence of long-term unemployment – persons unemployed 12 months and over, 1994



Source: OECD, Employment Outlook

"Intelligent" reduced Working Time is a Proactive Labour Market Policy⁴

Some-times it is proposed that the huge unemployment in Europe could be reduced by a general reduction in the working time. But to obtain a successful result from reducing the general working time, one of the conditions is that the European labour markets are not too inhomogeneous.

The above mentioned issues about the inhomogeneous European labour markets indicate that a general reduction in working time would be quite problematic. And when one also remembers the large geographical differences in unemployment in many countries and further more the differences in unemployment which arise from the skill structure, the conclusion is that a general reduction in working time is precisely a too general tool to use to reduce unemployment.

But this does not mean that other kinds of rearranging the working time could not be used to achieve the goals of both lowering unemployment and also improving the functioning and flexibility of the labour markets. Leave-schemes - either for sabbatical, parental or educational purposes - could be such solutions.

Leave-schemes are a flexible reduction in annual working hours which can be targeted to special groups on the labour market. With leave schemes it is also possible to vary working time over the individual person's career. Especially the educational leave has even more interesting perspectives because this flexible reduction of working time achieve several goals in one time.

Through rotation with other persons on the labour market it is possible to get a flexible share of working time with an educational - intelligent - element. This gives an important contribution to obtain a reduction in the structural problems on the labour market and by that to increase the employment level on a permanent basis.

In Denmark leave schemes have existed since 1993. The educational leave scheme is today the most used scheme in Denmark, while the sabbatical leave scheme has only had a minor use. In 1996 approximately 1.2 per cent of the labour force is - calculated on a yearly basis - participating in the educational leave schemes.

⁴This discussion is also part of a paper from ECLM, which was made on request of Stuart Holland, ARIES, London, a paper in which we analyse and make simulations of the consequences of reducing annual working hours in Europe.

Another interesting element with the educational leave scheme model - which is appreciated by a majority of the social partners - is that this working time proposal with an educational investment strategy is an effective answer in the situation where more internationalisation and competition will give a pressure downward on some of the wages and prices we know today. That is why investment in improving the human resource basis is even more important when one has the ambition of maintaining and creating good jobs with good wages.

And finally, a higher aim at improving the educational skills of the labour force and to raise labour market training is also important because the renewal of the labour force will gradually be reduced. Because of the demographical development the supply of young and well educated persons will be relatively smaller in the future. To continuously improve the qualifications and training of the labour force it will gradually be more and more important in the future, that the people who have been on the labour market for some years get their qualifications up-dated.

Conclusion

To increase employment in Europe it is important that the European countries cooperate in designing a more active framework for the macroeconomic and labour market policies. Fiscal and monetary policies in the European countries have to be better coordinated to achieve the highest possible growth rates and a higher permanent employment level without the risk of increasing inflation rates.

In order to achieve this it is probably important that the large economic interaction between the European countries is better in-cooperated in the way economic policies today are planned and realized.

What Europe urgently needs is a higher internal demand, especially a higher investment share, supported by an improvement in the functioning of the labour markets, which first and foremost requires more active labour market policies, especially in human capital investments. To take some of the pressure of monetary policy to keep inflation down, more competition on the goods market will also help.

What Europe further needs is simply more focus on employment. Hopefully this will be one of the outcomes of the Intergovernmental Conference, so that The Economic and Monetary Union could be shortened to the three capital letters - EMU - in stead of the actual eMU. The e in eMU is deliberately written with a small letter because the monetary cooperation in the Maastricht Treaty is much

more developed than the employment part which almost have been left out in the cold.

What Europe can not benefit much from are the recommendations from The European Monetary Institute which were mentioned in the beginning of the paper. It is a kill to the effort and ambitions of achieving a higher permanent employment level when the members of the EMI state that unemployment in Europe today is almost entirely structural. This statement is further more made without any serious analysis of the structure of the unemployment situation in Europe of today.

More information and more knowledge can be achieved from the EU-Commission study, "The composition of unemployment from an economic perspective" where it is said that: "The concept of NAIRU (non-accelerating inflation rate of unemployment) is undoubtedly attractive from a theoretical point of view but its empirical estimation is so fragile that the concept becomes unusable operationally".

And further more it is said in the study from the EU-Commission: "Thus, the 9% (or so) of total classical unemployment could be reduced to about 6% in the frame of a strong, investment-based growth process by those who are quickly employable with limited efforts of retraining when jobs become available in periods of fast expansion of effective and potential output. The remaining structural part, however, can only be absorbed with the help of structural policies: retraining, active labour market policies, and the creation of adequate working posts without which these policies would not be able to reach their full return and would be a source of disillusion for the beneficiaries of all these efforts if, as before, they are unable to find a job"

Most of the European countries have the same kind of macro economic problems, first and foremost a lack of sufficient working posts. This is a problem which probably can be more easily solved when is it realized that Europe is an entity. An entity which on the one hand can keep unemployment levels continuing high or if used in an offensive matter can contribute to reduce unemployment more effectively in a medium and a long term.

Notes

1) **An European National Account:** In calculating the contributions to growth for Europe as an entity we use data from the latest OECD Economic Outlook no 59. Some of the figures which are shown in table 1- 2 are also calculated by OECD. When one compares the aggregates in the OECD-outlook with the calculations from ECLM one can find minor differences.

The reason for these differences is that we use a different weighting scheme. OECD uses fixed GDP weights. These weights are based on 1991 purchasing power parities. This has the effect that a country like Turkey gives a quite large contribution to the development in the figures for OECD-Europe.

In our calculations of an European National Account we use current nominal weights in common currency based on the share from the previous year. We also use variable specific weights when we calculate the different aggregates. Current nominal GDP weights are used in calculating GDP growth rates. Nominal private consumption weights are used when we calculate growth rates for OECD-Europe private consumption and its contribution to GDP growth. The same principle is used for the other demand variables. And we have excluded data for Turkey in our calculations of the European National Account.

2) **HEIMDAL (Historical Estimated International Model of the DANish Labour movement)** is developed in The Economic Council of the Danish Labour Movement. The HEIMDAL model is a representation of the world economy from a Danish/Nordic point of view. The model contains 13 OECD-countries and 3 non-OECD aggregates. The 13 countries are Denmark, Sweden, Norway, Finland, Germany, United Kingdom, France, Italy, Netherlands, Belgium, Spain, United States and Japan. The 3 aggregates are the four Asian NIC's (Korea, Taiwan, Singapore and Hong Kong), the OPEC-countries and the former USSR plus the Eastern European countries.

The three non-OECD aggregates are treated exogenous. Each OECD country is described by about 100 equations. The structure of the model makes it possible to make calculations about a single country or several OECD aggregates, for instance EU, the Nordic countries and so on. The HEIMDAL model as a whole contains 1400 equations and 2500 variables.

The individual country models is divided into the following sub-models:
Household sector,
Business sector, Labour market, Domestic prices, Foreign sector, Public sector and Financial sector

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⁵Translated to English: "The importance of monetary policy in Germany in Europe of today"



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