

**Political and economic reforms on the path to euro adoption: The case of
Spain, Greece, Slovenia and Slovakia**

By

Cherine Mekkaoui

A thesis submitted to the Faculty of Graduate and Postdoctoral Affairs in partial fulfillment of the
requirements for the degree of

Master of Arts

In

European, Russian and Eurasian Studies

Carleton University
Ottawa, Ontario

© 2012
Cherine Mekkaoui



Library and Archives
Canada

Published Heritage
Branch

395 Wellington Street
Ottawa ON K1A 0N4
Canada

Bibliothèque et
Archives Canada

Direction du
Patrimoine de l'édition

395, rue Wellington
Ottawa ON K1A 0N4
Canada

Your file Votre référence

ISBN: 978-0-494-91566-0

Our file Notre référence

ISBN: 978-0-494-91566-0

NOTICE:

The author has granted a non-exclusive license allowing Library and Archives Canada to reproduce, publish, archive, preserve, conserve, communicate to the public by telecommunication or on the Internet, loan, distribute and sell theses worldwide, for commercial or non-commercial purposes, in microform, paper, electronic and/or any other formats.

The author retains copyright ownership and moral rights in this thesis. Neither the thesis nor substantial extracts from it may be printed or otherwise reproduced without the author's permission.

AVIS:

L'auteur a accordé une licence non exclusive permettant à la Bibliothèque et Archives Canada de reproduire, publier, archiver, sauvegarder, conserver, transmettre au public par télécommunication ou par l'Internet, prêter, distribuer et vendre des thèses partout dans le monde, à des fins commerciales ou autres, sur support microforme, papier, électronique et/ou autres formats.

L'auteur conserve la propriété du droit d'auteur et des droits moraux qui protègent cette thèse. Ni la thèse ni des extraits substantiels de celle-ci ne doivent être imprimés ou autrement reproduits sans son autorisation.

In compliance with the Canadian Privacy Act some supporting forms may have been removed from this thesis.

While these forms may be included in the document page count, their removal does not represent any loss of content from the thesis.

Conformément à la loi canadienne sur la protection de la vie privée, quelques formulaires secondaires ont été enlevés de cette thèse.

Bien que ces formulaires aient inclus dans la pagination, il n'y aura aucun contenu manquant.

Canada

ABSTRACT

Member states of the Eurozone are undergoing a turbulent period both domestically and internationally. On the national front, many countries, including Greece and Spain, have been led to early elections or the collapse of their government as a result of the serious financial and economic crisis. Reforms have been hailed as the panacea to the affected member state's woes. These reforms have mainly addressed the need to reduce costs, often via labour market reforms.

When analyzed in detail, the countries which are now under scrutiny did not undertake these necessary reforms during times of economic prosperity. Political determination for change was not matched by willingness to upset the civil society in the short term. Far-reaching measures must now be implemented in the labour markets and taxation policy convergence should be explored. Only real reform can ensure a future for any member state within the Eurozone.

ACKNOWLEDGEMENTS

The writing of this thesis has undoubtedly been the most significant, challenging and rewarding academic journey that I have ever embarked upon.

This thesis would not have been possible without the guidance of my advisor, Dr. Crina Viju. I am grateful for her input, patience, encouragement and support throughout this process.

I am indebted to my parents for their continued support during my studies, my time abroad and throughout the completion of this project.

I would like to thank EURUS and Carleton University for the opportunity to intern abroad and successively study abroad in Italy and Spain. Without these experiences, my knowledge of the Spanish language and subsequent primary research would have been very hard to acquire.

To my family and friends, thank you for your words of encouragement and support throughout this process, especially late at night.

Table of Contents

ABSTRACT

ACKNOWLEDGEMENTS

TABLE OF CONTENTS

LIST OF FIGURES

1 INTRODUCTION

1.1 LITERATURE REVIEW	8
1.1.1 Theoretical Literature Review	8
1.1.2 Empirical Literature Review	17

2 METHODOLOGY

3 CASE STUDIES

3.1 SPAIN	39
3.1.1 Political Forces	40
3.1.2 Structural Labour Reforms	47
3.1.3 Tax reform	55
3.1.4 Concluding remarks	59
3.2 GREECE	60
3.2.1 Political Forces	61

3.2.2	Structural Labour Reforms	71
3.2.3	Taxation.....	80
3.2.4	Concluding Remarks.....	83
3.3	SLOVENIA	84
3.3.1	Political Forces.....	86
3.3.2	Structural Labour Reforms	91
3.3.3	Taxation.....	99
3.3.4	Concluding remarks.....	100
3.4	SLOVAKIA	101
3.4.1	Political forces.....	101
3.4.2	Structural Labour Reforms	108
3.4.3	Taxation.....	117
3.4.4	Concluding Remarks.....	122

4 CASES COMPARISON

SUMMARY AND CONCLUSION

FURTHER RESEARCH

BIBLIOGRAPHY

LIST OF FIGURES

Figure 1: Unit Labour Costs among Non-Convergent MS.....	23
Figure 2: Unit Labour Cost by Industry Sector, Spain	24
Figure 3: Unit Labour Costs by Industry Sector, Greece.....	26
Figure 4: Unit Labour Costs in Selected Member States.....	27
Figure 5: Unemployment Rate, Spain VS OECD, 1970-2008	45
Figure 6: Unit Labour Cost Spain, 2000-2011	53
Figure 7 : Spanish Unit Labour Costs Per Industry, 2000-2008.....	54
Figure 8: Greek Government Spending, %GDP.....	65
Figure 9: Unit Labour Costs in the Eurozone, 1980-2007.....	76
Figure 10: Unit Labour Costs Greece, 2000-2010	77
Figure 11: Slovenian Wage Growth	91
Figure 12: Unemployment Rate, Slovenia vs. EU, 2000-2010	92
Figure 13: Share of Unemployed Slovenian Youth (15-24 years), Unemployed for 12 months or more	93
Figure 14: Ease of Doing Business in Slovenia, 2008	94
Figure 15: Unit Labour Costs Slovenia	95
Figure 16: Unit Labour Costs Slovakia	113
Figure 17: Comparison of Tax Rates Faced by Investors, Slovakia vs. Selected Countries	121
Figure 18: Comparison of Case Studies	124
Figure 19: ULC Comparison, Spain, Greece, Slovenia and Slovakia.....	127

1 Introduction

Overview

The global financial and economic crisis has wreaked havoc on countries big and small since the summer of 2007. The crisis that ensued was portrayed in the media as second only to the Great Depression. This association was made on the basis that the crisis beginning in 2007 shared similarities with the events that triggered the Great Depression. The European Commission (2009) explains these similarities as follows:

‘The crisis was preceded by[a] long period of rapid credit growth, low risk premiums, abundant availability of liquidity, strong leveraging, soaring asset prices and the development of bubbles in the real estate sector. Over-stretched leveraging positions rendered financial institutions extremely vulnerable to corrections in asset markets’ (Economic and Financial Affairs DG, 2009, p. 1).

The European Union, and especially its Eurozone member states, has been affected by a series of crises that followed one another. At the onset, the problems could be seen in the acute liquidity shortage that existed among financial institutions as markets demanded higher returns in exchange for rolling over¹ their debt. The solvency of financial institutions began being called into question, culminating with the collapse of Lehman Brothers in September 2008, causing investor panic and chaos in the stock markets as ‘value’ vanished. Up until this point, the EU was largely sheltered from the financial mismanagement unraveling in the United States. However, soon after, the financial woes trickled down to the real economy leading to reduced credit lending by banks to

¹To "roll over" a debt is to replace a debt due for payment with a new debt.

both businesses and consumers. Banks were even skeptical to trade between one another as no one knew or trusted what assets each bank held on its balance sheet and whether those assets were in fact substantiated or represented toxic assets cleverly disguised as sophisticated financial products related to the subprime crisis that had originated in the United States. This characterized the period referred to as the credit crisis. Businesses and households found it increasingly more difficult to secure loans from banks which led to a marked decrease in economic activity, which itself caused more panic, leading banks to be ever-more unwilling to lend, thus leading to a crisis that fed off of its cyclicity. The lack of financing contracted world trade and halted production. Confidence was at an all-time low, both for businesses and consumers. Central banks attempted to intervene by reducing interest rates to historical lows, in order to reduce the cost of commercial banks' financing. The move was intended to inject liquidity into the commercial banks, who were then supposed to pass on the savings to consumers and businesses. Unfortunately, banks that had seen their portfolios depreciate substantially in the stock market panic were not ready to return to business as usual. Meanwhile, in the Eurozone, in November 2009, Greece announced that its budget deficit was 12.7% of gross domestic product (GDP), more than twice the amount it had previously stated and four times the allotted amount of 3%, as specified by the fiscal requirements of Economic and Monetary Union (EMU) (BBC, 2012). This announcement marks the beginning of the sovereign debt crisis. Soon after Greece's announcement, Fitch, a ratings agency, reduced Greece's credit rating and ranked its outlook negative. Standard & Poor and Moody's, other ratings agencies, followed suit. The importance of these ratings refers back to the market for lending money to governments, or the issuance of government bonds. Investors are willing to accept a lower, stable interest on government bonds if they believe that the country is trust-worthy and the face value of the bond will retain its value until maturity. The inverse holds true for investors that

do not trust the credibility of countries, and in return for the increased risk they must bear to purchase these bonds, they demand higher interest payments. This is a simplified version of what occurred in Greece, despite government promises to undertake reforms in order to address its fiscal imbalances. Perhaps it was Greece's history with falsifying data in order to qualify for euro adoption, or the economic and social tensions that arose in Greece as reform and austerity measures were outlined, or even the lack of credibility that the government institutions held as a result of their track record with corruption that markets, and ratings agencies, distrusted the efforts of the government. So severe ran this distrust that in 2010, Standard & Poor's reduced Greek bonds to junk status sending a clear buyer-beware signal to the markets (BBC, 2012). Moody's quickly followed, echoing the junk status verdict. On May 2, 2010, Greece, the Eurozone member states, and the IMF agreed to a €110 billion bailout plan for Greece (BBC, 2012). The Eurozone provided €80 billion and the IMF €30 billion. Later that month, an austerity package narrowly passed in Spain's parliament. Spain, which was reeling from the collapse of its construction and housing market, also came under the spotlight. Despite the €15 billion in cuts, Spain's rating was also reduced, though not as quickly or as low as its Greek counterpart. The markets and ratings agencies seemed to have decided that contagion was spreading quicker than the EU was letting on.

The question has often been asked about what the Eurozone leaders were doing in order to mitigate some of the negative press and associated externalities. The cynical answer can be summarized as organizing summits in order to give the impression that they (generally speaking, Germany and France) stood in defence of their beleaguered Eurozone members. In practice, the answer is a bit more complicated. The European Central Bank (ECB) is prohibited by law from directly intervening to bailout any one member state's economy. As a result of this parameter, instated in order to safeguard the ECB from political pressures, any concrete decisions taken by Trichet (the

now-former president of the ECB) and the rest of the EU finance ministers had to be carefully devised and worded. What came about in May 2010 as a response was the European Financial Stability Facility (EFSF), a temporary bailout mechanism (Turner, 2011). In March 2011, with markets not yet calm, the EFSF's powers were extended allowing it to buy debt in primary markets. Later in the same month, the realization that the Eurozone may require permanent help was institutionalized with the EU's finance ministers' decision to create a permanent bailout mechanism, the European Stability Mechanism (ESM) (WSJ, 2012). National tensions, brewing since the start of the Greek saga, finally erupted costing some Eurozone politicians support in their member states and leading some to electoral defeat.

An unpublicized meeting in May 2011 between the finance ministers of Spain, France, Germany and Italy prompted speculation that the countries were devising a process by which Greece would be asked to leave the euro. No such procedure exists in the treaties, though the procedure for joining monetary union is extensively detailed. This can be interpreted as the explicit intention of the architects of monetary union, who saw the adoption of the euro as an irrevocable step in the process to completing EU integration. Greece was not asked to leave the Eurozone following the recess of the impromptu meeting, but it was made clear that Greece was to immediately implement substantial reforms in order to continue receiving support from the Eurozone members, the ECB and the IMF (referred to collectively as the *troika*). Though the possibility of restructuring Greece's debt was dismissed at this time, it became apparent throughout the summer and fall that the budgetary cuts and reforms passed by Greece would not suffice to alleviate pressure. In October 2011, Eurozone leaders settled that it was time to revisit the restructuring of Greek debt. Holders of Greek debt were asked to take a 50% haircut on the value of their holdings (WSJ, 2012). By November, debt yields across the Eurozone had risen dramatically as investors became

increasingly uneasy watching the Eurozone try, but fail, to resolve the crisis. The following month, in a move intended to reassure investors, the Eurozone leaders alongside other EU member states agreed to greater centralization of their budgets and automatic punishment for those who break the budget accord. This re-iteration did not assuage the markets and yields, particularly Spanish and Italian, continued to soar. Thankfully, the EFSF's auction days later of 3-month treasury bills was met with success and managed to temporarily calm markets. Respite was short and in January 2012, Standard & Poor's downgraded the credit rating of the EFSF itself, citing the deteriorating economics of the EFSF's contributors (WSJ, 2012). The ECB, a vocal opponent of Greek restructuring, insisted that it would not agree to a write-down of its own Greek debt holdings but in February exchanged its Greek bonds below par value in an effort to secure a deal between Greece and its creditors. By late February, the debt deal² was settled and Greece entered into its debt swap plan with private creditors. Following the deal and swap, Standard & Poor's declared that it considers Greece to be in default on its sovereign debt obligations launching long, heated and ongoing debates by politicians, academics and pundits on whether the debt restructuring does represent a default.

On March 20, 2012, Greece voted to accept the second round of its bailout funds, signifying that despite social unrest, it also accepts to implement the reforms demanded by the EU, ECB and IMF finance ministers. On March 30th, Greece announced that it may require a third bailout.

² Details of the plan include: current creditors agreeing to lose 53.5% of the face value of their debt to satisfy the IMF; the ECB and other European central banks take no loss on debt holdings with any profit made on the holdings transferred to Greece; a lower interest rate on new debts; and the oversight of a debt servicing account by official creditors.

The onset and worsening of the crisis has focused attention on how affected countries wound up in such a precarious situation. This has led the debate to the importance of addressing structural issues and implementing the reforms necessary to respond to economic shocks. The crisis has served to highlight existing structural weaknesses which have been left unaddressed in Member States. It is important to make the distinction that the resulting economic environment has not been caused by the financial-turned-economic crisis, but that the crisis has brought to the forefront pre-existing issues that can no longer be ignored by the Eurozone member states.

Objective

This thesis examines the political and structural changes in Spain, Greece, Slovenia and Slovakia on their paths towards adopting the euro. These four countries were chosen because they share similar socio-economic characteristics and have undergone transition from authoritarian rule to democratic societies. Moreover, they are all peripheral member states of the Eurozone. This thesis seeks to determine what, if any, are the similarities of reforms undertaken in order to qualify for the euro and the affect the reforms had on the member states once they obtained Eurozone membership. Secondly, this thesis also looks to determine whether two of the newest Eurozone member states, Slovakia and Slovenia, pursued similar or different reforms from those of Spain and Greece in an effort to gauge whether the newer member states converged to the reforms process of the older member states or chartered out a new path for themselves. Drawing parallels or divergences from the experiences of new versus old member states can be important in forecasting trends for future adoption of the euro. This is important because member states which have joined the EU from 2004 onward are under the obligation to adopt the euro once they are ready. This requirement is different from that of older member states, such as the UK and Denmark, which have 'opt-out' clauses built into their EU accession agreements for reasons of

economic sovereignty. As all new member states will have to adopt the euro, it is important and beneficial that they review the successes and failures of other member states to learn from, not repeat, their mistakes.

Division of thesis

The following section will examine the literature on the theoretical and empirical contributions to EMU. The second section will focus on the methodology implemented to examine this topic, followed by the four case studies on Spain, Greece, Slovenia and Slovakia. The findings of the case studies will be summarized and compared in the subsequent section. The fifth section will offer a summary of the research undertaken and its contribution. Finally, the sixth section offers areas of further research.

1.1 Literature Review

This section is divided into a theoretical literature review exploring selected economics theories and an empirical literature review aimed at contributions on political and structural forces, such as labour and taxation reforms.

1.1.1 Theoretical Literature Review

The theoretical review focuses on Economic and Monetary Union (EMU) looking at the theories on optimum currency areas (OCA), the benefits and costs of EMU and the Stability and Growth Pact (SGP). These three areas are essential to understanding the reasoning and motivation behind the formation of the Eurozone.

1.1.1.1 Economic and Monetary Union

Optimum Currency Areas

The theory on optimum currency areas (OCAs) is often found in literature on the formation of the EMU. The term was coined by Mundell (1961) in his influential paper, “A Theory of Optimum Currency Areas”. Broz (2005, p. 55) explains that though the idea of exchange rate regimes in academia pre-dated Mundell’s paper, his work represented the first instance where someone suggested that a currency area ‘should be a region, whose borders need not necessarily coincide with state borders.’ Indeed, Mundell sought to explain when it was appropriate for countries to join together and what characteristics a common currency area should embody. Mundell (1961) placed emphasis on the mobility of factors, especially labour, as an important determinant in the formation of an OCA. Mundell (1961, p. 659) stated that ‘if the exchange rate regime within a region causes unemployment in one part of the region, or if it forces another part of the same region to accept inflation as the cure for unemployment, then this regime is not optimal’. Price and wage flexibility

are also stressed in Mundell's (1961) theory. Though elaborated in much finer and more extensive detail than we have the scope to do here, Mundell's theory has served as the starting point for the development of literature on the Eurozone as a common currency area.

Broz (2005) reviews the many contributors that have added to and expanded upon Mundell's original theory.

McKinnion (1963) expanded upon Mundell's theory on OCA, citing the 'degree of openness as a crucial criterion in forming the OCA and defines it as the ratio of tradable to non-tradables' (Broz, 2005, p. 56). McKinnion's addition is based on the idea that the more open an economy is, the more advantageous it becomes for it to have a fixed exchange rate or participate in a currency union. The opposite holds true in the case of a closed economy. Broz (2005) summarizes that a small open economy would find it advantageous to join a larger common currency area.

Kenen (1969) expanded the point of factor mobility, stressing that:

'When regions are defined by their activities, not geographically or politically, perfect interregional labour mobility requires perfect occupational mobility. And this can only come about when labour is homogenous (or the several regions belonging to a single currency area display very similar skill requirements). In consequence, Mundell's approach leads to the sad certainty that the optimum currency area has to be small. It must, indeed, be coextensive with the single-product region' (Kenen, 1969, p. 44).

Kenen (1969) introduced another important variable to the theory on OCA- that of product diversification. Broz (2005) explains that this came as the result of Kenen's disbelief in perfect labour mobility. In fact, Kenen (1969) went so far as to suggest that "diversity in a nation's product

mix, the number of single-product regions contained in a single country, may be more relevant than labour mobility” (p. 49). Kenen also provides the notion that if a ‘diverse shock hit[s] a common currency area, fiscal integration between regions can mitigate the impact through fiscal transfers between regions’ (Broz, 2005, p. 59).

Broz (2005) contributed that Kenen’s diversification idea is closely related to McKinnon’s openness criterion.

Cordon (1972) introduced the idea that monetary and exchange rate policy control would be lost once countries joined the common currency area. We know this to be the case in the Eurozone, as member states have conceded their control over their monetary policy to the European Central Bank. Cordon (1972) considered wage and price flexibility to be the most important criteria in forming a common currency area due to their ability to quickly respond to asymmetric shocks (Broz, 2005).

Mundell (1973) restated the importance of factor mobility but introduced the notion that a financially integrated union can withstand asymmetric shocks (Broz, 2005).

According to Broz (2005), Ishimaya (1975) was among the first to suggest that OCA should be based on multiple, not one, criteria and that each country that was contemplating joining an OCA needed to evaluate its own costs and benefits.

With the emphasis on deepening integration within the EU in the 1980s and 1990s, the theory on OCA was revived, especially as regards to justifying a common currency. The Commission of the European Communities’ (1990) report “One Market, One Money” touched on some potential

issues but after emphasizing the benefits of a common currency recommended further monetary integration.

Over time, the variables that contribute to the analysis of the OCA have changed, morphed and multiplied as authors have pointed out the problems with one or more factors leading to a flexible understanding of what an OCA is comprised of.

Benefits and costs of a currency union

The benefits and costs of forming or joining a currency union have received much academic thought.

The main benefits, as described by Obstfeld and Roggoff (1996) include:

‘Reduced transaction costs from currency conversion; reduced accounting costs and greater predictability of relative prices for firms doing business in the countries forming the currency area; insulation from monetary disturbances and speculative bubbles that might otherwise lead to unnecessary temporary fluctuations in the real exchange rates (given sticky domestic prices); and less political pressure for trade protection because of sharp shifts in the real exchange rates’ (Broz, 2005, p. 70).

Addressing the EU particularly, an additional benefit for the new member states would be that they could ‘import credibility to the extent that the credibility of the single monetary policy is regarded as greater than the monetary policy of the individual country’ (Townsend, 2007, p. 247).

Crowley (2000) added that the drive towards euro adoption may promote reforms, for instance in the areas of fiscal institutions and transparency, deregulation or incomes policy which could lead to higher growth and better living standards for the society as a whole.

The costs of a currency area are also numerous.

Costa and De Grauwe (1999) cite that limited policy instruments in times of economic downturn among the most salient problems. Following currency union, and in the case of the EU, the European Central Bank holds sole custody of monetary policy and only acts in the best interest of the entire currency area.

Another drawback is related to the different economic cycles of EU member states which can find themselves at different stages in the cycle between boom and recession. The creation of a single currency removes the policy option to set interest rates separately at the level appropriate for each country (De Grauwe P. , 2003).

Monetary union requires a high degree of labour mobility. A lack of labour mobility can lead to a regionalization between depressed areas characterized by high unemployment and flourishing areas of high incomes (De Grauwe P. , 2003). In a currency area that is not homogenized across economic, social and legal dimensions, regionalization may become the norm. The concentration of economic activity can contribute to another cost- the development and persistence of asymmetric shocks³ (Costa & De Grauwe, 1999).

Additionally, the actual monetary cost, though one-time, of converting all of the price tags, bank accounts, computer software and programs and the re-education of citizens and staff cannot be

³ Refers to a situation where an economic supply or demand shock affects only a particular country in a common currency area. Asymmetric shocks are problematic because they hinder a central bank's ability to devise a beneficial monetary policy for all common currency members.

neglected. Though, evidently, this would be seen as a sunk cost, it still represents a cost that countries must absorb.

The logic of OCA dictates that if the benefits outweigh the costs, then countries should move forward and create a common currency area. According to Dyson (2000) the classic features of the OCA- labour mobility, flexible labour markets, and synchronized business cycles- were not present across the countries that chose to establish the EMU, but the choice was made to go ahead with a union. Indeed, Issing (2008, p 11) states that ‘thus the majority of economists were agreed in their evaluation of the monetary union from the economic perspective: this group of 11 countries represented anything but an optimum currency area’.

Since the requisites for an OCA were not fulfilled by the 11 countries that chose to enter into monetary union, we must conclude, as Capie and Wood (2003) do, that the choice was politically motivated. That this decision was based on the belief that EMU would be justifiable *ex post*, as suggested by Vieira and Vieira (2010), is likely. It can be reasonably assumed that EU politicians choosing to enter into EMU did so expecting that trade and business cycles would converge once monetary union was in place, a simplistic view of the endogeneity⁴ theory of OCA.

Economic and Monetary Union

Critics were very quick to point out that the Eurozone is not an OCA, and policy makers did not really dispute that fact. Since the Eurozone is not an OCA, joining the economic and monetary union (EMU) and adopting the euro was not based on the criteria elaborated by the various

⁴ An OCA is endogenous if, once the currency union is formed, trade integration between its members increases, which leads to synchronized business cycles.

contributors to OCA theory. Instead, a list of convergence criteria was established. Even if the establishment of the common currency was a politically motivated decision, economic measures are used to determine whether a country can or cannot participate.

For any new prospective Eurozone member state the way toward adopting the euro involves two steps. First, each EU member state has to participate in the Exchange Rate Mechanism (ERM) II for at least two years. This refers to the exchange rate arrangement established on 1 January 1999 that provides a framework for exchange rate policy cooperation between the Eurosystem and EU Member States whose currency is not the euro (European Central Bank, 2011). This involves pegging their currency to the euro with a standard fluctuation band of $\pm 15\%$, though a narrower band may be agreed on request (European Central Bank, 2011).

The second step refers to fulfilling the other Maastricht criteria specified by the Treaty on EU (TEU). The country in question can become an EMU member and adopt the euro once both steps have been completed. The Maastricht criteria refer to five basic policy objectives, as summarized by Crowley (2002):

1. Inflation of no more than 1.5 percentage points above the average rate of the three EU member states with the lowest inflation over the previous year,
2. Long-term interest rates should be no more than two percentage points above the rate in the three EU countries with the lowest inflation over the previous year,
3. The currency has to participate for at least two years in the European mechanism of exchange rates ERM II, and respect the normal fluctuations margins of this mechanism,

without severe tensions on the foreign exchange market and without devaluations at its own initiative,

4. A national budget deficit at or below 3% of gross domestic product (GDP),
5. National public debt not exceeding 60% of GDP. A country with a higher level of debt can still adopt the euro provided its debt level is falling steadily.

As Lavrac (2004) summarizes, ‘Maastricht convergence criteria can be divided in three monetary and two fiscal convergence criteria. Overall they measure nominal convergence, degree of harmonization of macroeconomic – fiscal and monetary – policies’ (Lavrac, Fulfillment of Maastricht Convergence Criteria and the Acceding Countries, 2004, p. 1).

When the Maastricht Treaty was concluded in 1992, the United Kingdom and Denmark were granted an opt-out⁵ clause which meant that they were not required to participate in the third stage of EMU and consequently introduce the euro (Institutional and economic framework of the euro, 2006). The twelve new member states (NMS) which joined the EU since 2004 do not have an opt-out choice and must adopt the euro under the Treaty. The choice to adopt the euro can only be taken once a member state satisfies the Maastricht requirements of nominal convergence.

Literature on monetary unions reflects that explicit fiscal constraints are necessary for its survival. ‘Fiscal profligacy could lead to pressure being exerted on the European Central Bank to inflate away part of a country’s debt burden, or could involve pressures on other national governments to

⁵ Although Sweden did not formally negotiate an opt-out clause on the euro, it does have a special understanding with the Commission and the ECB that it will not introduce the euro without a positive referendum (a referendum on the euro failed in 2003).

bail-out the country with the debt problem' (Barry, 2001, p. 7). Having fiscal constraints in place circumvent the situation whereby the European Central Bank would find itself in a position of political pressure, putting the needs of one country ahead of the union. Even if a 'no-bail-out' policy exists, as Buiter et al. (1993) argue, that alone does not preclude the ECB from being called upon in extraordinary circumstances.

De Grauwe (1997) argues though that in EMU budget deficits cannot be financed by money creation so monetary union represents a strengthening of the budget constraint.

Buiter et al. (1993) suggest that the adoption of external fiscal commitments, as occurs when member states join the euro, could provide a way around the domestic factors that systematically induce excessive deficits and ratchet up current spending. Certainly, criteria regulating the fiscal and monetary policies of national governments cannot be expected to deal with the systematic problems that persist in each member state. Criteria addressing the causes of issues like unemployment and tax evasion are needed as a complement to the criteria analyzing the symptoms, as exemplified by interest rates, debt and deficit. Unless the underlying problems are addressed, the macro indicators cannot and will not improve.

The Stability and Growth Pact

The Stability and Growth Pact (SGP) is an agreement that was adopted in 1997 to provide a framework for coordination of national fiscal policies in EMU. The SGP was intended to monitor the Member States' compliance with the Maastricht convergence criteria. The SGP is made up of a preventative and a dissuasive arm. The preventative side requires member states to submit annual stability or convergence programs which highlight how they will continue to maintain sound fiscal positions, which are then analyzed by the Commission. The Commission decides whether the

programs are satisfactory or whether to issue a warning to the Member State that it needs to realign policies in order to avoid excessive deficit. The dissuasive arm is based on the excessive deficit procedure (EDP), which is triggered if a Member State's deficit exceeds 3% of GDP. This leads to recommendations to address the issue in a timely manner, and in the case of non-compliance to sanctions. Regrettably, consistent enforcement of the SGP has lacked in the past and the SGP itself has come under heavy criticism. Regarding inconsistency, the Council of Ministers who are tasked with enforcing sanctions, failed in 2003 to discipline France and Germany when they breached the Pact, but fined Portugal in 2002 and Greece in 2005 (González-Páramo, 2005).

In 2005, the SGP was reformed to reflect that determining to launch the EDP would be based on a number of factors affecting a member state's fiscal state such as the cyclicity of its budget, its debt level and the type and duration of the member state's crisis. This reform was seen to weaken the character of the rigid SGP and served to support the criticisms of a double standard for larger, more powerful Member States.

Most recently, a reform was begun in 2011 which would introduce a fiscal treaty and is being touted as a successor for the failed SGP.

1.1.2 Empirical Literature Review

The empirical literature review examines contributions regarding political and structural forces such as labour and taxation reforms, factors which are examined in the case studies that follow.

Political

The reasons leading to the creation and adoption of the euro are widely documented. Otmar Issing⁶ (2008, p. 47) dedicated an entire book to the birth of the euro, where he states clearly that ‘the selection of participants ultimately remains a political decision’ and that ‘nine years on, the necessary conditions of monetary union have by no means been fully achieved’. Reviewing the theoretical background, Issing (2008) concludes that ‘thus the majority of economists were agreed in their evaluation of the monetary union from the economic perspective: this group of eleven countries represented anything but an optimum currency area’ (Issing, 2008, p. 47).

Since the case could not be organically made on the basis of economic theory relating to currency unions, national politicians had to conceive of a way to sell the new currency to their citizens. The case had to be made that, upon surrendering their national currency, greater benefits would follow. Politicians had to frame the euro issue in terms of national policy discourse. Hooghe and Marks (2008, p. 9) explain that ‘European issues have entered party competition. On major issues, governments, i.e., party leaders in positions of executive authority, try to anticipate the effect of their decisions on domestic politics. Public opinion on European integration has become a field of strategic interaction among party elites in their contest for political power.’

The Eurozone was seen as a prestigious club whose membership was highly valued by politicians in Spain, Greece, Slovakia and Slovenia. Partaking in the Eurozone would solidify these peripheral countries’ positions within the EU itself and was a means to complete their process of

⁶ Chief Economist and member of the Executive Board of the European Central Bank from 1 June 1998 to 31 May 2006

‘Europeanization’⁷. Belonging to an exclusive collective like the Eurozone would also bring enhanced credibility, even if only by association.

Spain and Greece were motivated to adopt the euro as quickly as possible. Spain had its fiscal and monetary house in order and joined in 1999, while Greece had to wait until 2001 to qualify, though its entry is now highly disputed.

For Slovakia and Slovenia, timing was an important issue as they each chose different reform paths on their road to the euro. This variable approach is noted in Šmídková et al. (2003), where they agree that the appropriate speed for adoption should be assessed on a case-by-case basis, a departure from the older member states that sought to adopt the euro as quickly possible. They state that:

‘Rapid entry could be beneficial for a country that does not have an established tradition of domestic monetary policy or for a country that has made significant progress with real convergence. More prudent timing for Eurozone entry would be better for a country that has a credible monetary policy, that still has a significant amount of real convergence in front of them and that does not have a very flexible economy’ (Šmídková et al. , 2003, p. 22).

Here, we begin to frame the choice of adopting the euro from the perspective of the member joining- does it make sense for the country to give up the flexibility of monetary policy or is it in its best interest to wait until significant progress has been made to reflect real convergence? Joining the euro no longer carries the expectation of Europeanization, instead, Europeanization from within (national reforms first) is seen as the pre-cursor to the successful adoption of the euro.

⁷ Refers to the assimilation of a certain set of values espoused by the European Union and the European project

Paul De Grauwe (2009, p. 172) argues that the long-term success of the Eurozone is contingent on the ‘continuing process of political unification’. He explains that this is needed to deal with divergent economic movements but also to address the flaws in the governance of the Eurozone. That particular flaw, he says, is that ‘while national politicians continue to bear the political responsibility for unfavourable economic developments, key instruments to deal with these have been transferred to European institutions that bear no political responsibility for their decisions’ (De Grauwe P. , 2009, p. 169). His thesis is ever relevant in the wake of a series of crises that have overturned politicians and governments alike.

De Grauwe (2009) states that the degree of political integration affects the optimality of a monetary union, citing taxation policies amongst the examples where asymmetric shocks of political origin (increasing or decreasing taxes) would be better contained with enhanced political integration.

In fact, De Grauwe (2009) is skeptical of the effectiveness of structural reforms alone. If national politicians have to endure the sole responsibility for unemployment, he argues, it is only natural that they will want to use all available instruments to fight unemployment. He argues that:

‘One cannot maintain a political system where national politicians are made fully responsible for unemployment while key instruments to deal with this problem have been taken away from them, and are held by those who do not want to be made accountable for this problem. Not only wage policies have remained in the hands of national governments, the whole of social policies together with the structural reform processes are national affairs. These create a potential of structural divergences between member states leading to diverging trends in output and employment’ (De Grauwe P. , 2009, p. 168).

Using the example of unemployment, a salient one for all four case study countries, De Grauwe highlights one of the most pressing problems in the EU- that national politicians are often held responsible for issues that affect their countries but may not be fixable without further political integration and support. Of course, further integration blurs the line between national sovereignty within the EU.

Labour

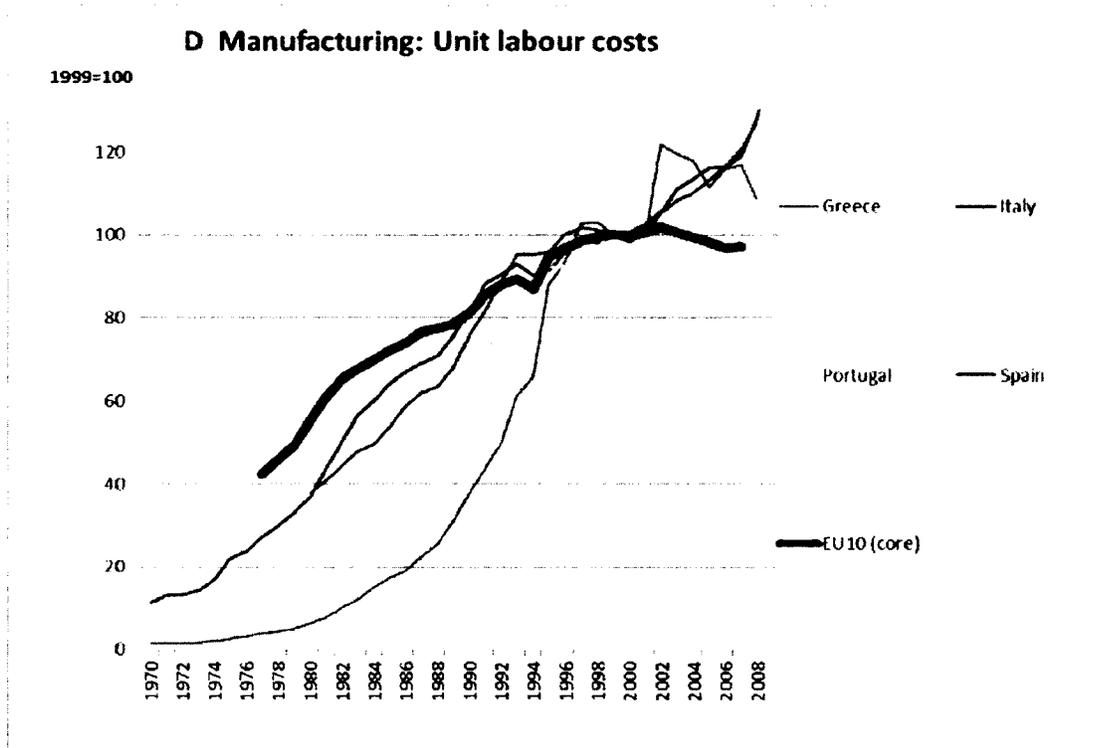
Eamets and Masso (2004, p.4) elaborate that ‘labour market flexibility shows how quickly markets adjust to the external shocks and changing macroeconomic conditions.’ This underlines the importance of labour market flexibility for the greater functionality of an economy. A country whose labour market exhibits high flexibility, as defined in 1987 by Klau and Mittelstadt across four broad aspects⁸, has the ability to deal with economic instability in a swift and decisive manner, allowing for the containment of negative externalities. A country that does not possess a flexible labour market may find itself held hostage by strong labour unions in times of economic uncertainty, or at a loss for policy direction when faced with a labour population that cannot or will not move across industries or geographic barriers. Indeed, the particularities of a member state’s labour market are central to its success and future within the Eurozone.

A study conducted by Ecorys, a research and consulting company, on behalf of the Directorate General (DG) of Enterprise in 2011 showed that while unit labour costs have converged for some members of the Eurozone, for others unit labour costs have increased, especially ‘when the implications for competitiveness represented by that trend could not be offset by a depreciation in

⁸ (1) Real labour cost flexibility at the economy-wide level; (2) Adaptability of relative labour costs across occupations and enterprises; (3) Labour mobility; (4) Flexibility of working time and work schedules.

each country's currency against (say) the deutschemark, unit labour costs (ULC) continued to increase more rapidly than the EU10 average' (Ecorys Nederland BV, 2011, p. 9). The report states that not only did unit labour costs not decrease as a result of better resource allocation in Greece and Spain particularly, but costs continued to increase in these countries when they began to decrease for the average of the EU10. Figure 1 depicts the trend in labour costs. We can note a convergence from 1994 until 1999-2001, the period of euro adoption for the first and second waves of currency change. By 2002, with Greece and Italy joining the euro, we begin to see a strong divergence from the EU10, with unit labour costs starting to rise, most drastically in Greece. This can be interpreted as a deterioration of competitiveness for Greece and Spain, alongside Italy and Portugal. As unit labour costs rise, a product becomes more expensive, and its appeal to consumers decreases. Manufacturers will tend to seek a location for production that has a lower unit labour cost in order to maximize their profit margin. While unit labour cost is by no means the only factor, it is certainly a determining variable, especially since the EU's reduction of barriers on imports from China.

Figure 1: Unit Labour Costs among Non-Convergent MS



Source: ECORYS Nederland BV, 2011

The report also found that in new member states, like Slovakia, joining the euro led to some convergence of productivity in key manufacturing sectors. In the case of Slovakia, this is best exemplified by the emergence of the automotive production industry within the country. Furthermore, the report suggests that there is some evidence of a Balassa-Samuelson effect⁹ in Slovakia, which the authors note is ‘in line with the prediction that the Balassa-Samuelson effect is especially strong for countries in a catching-up phase’ (Ecorys Nederland BV, 2011, p. 13).

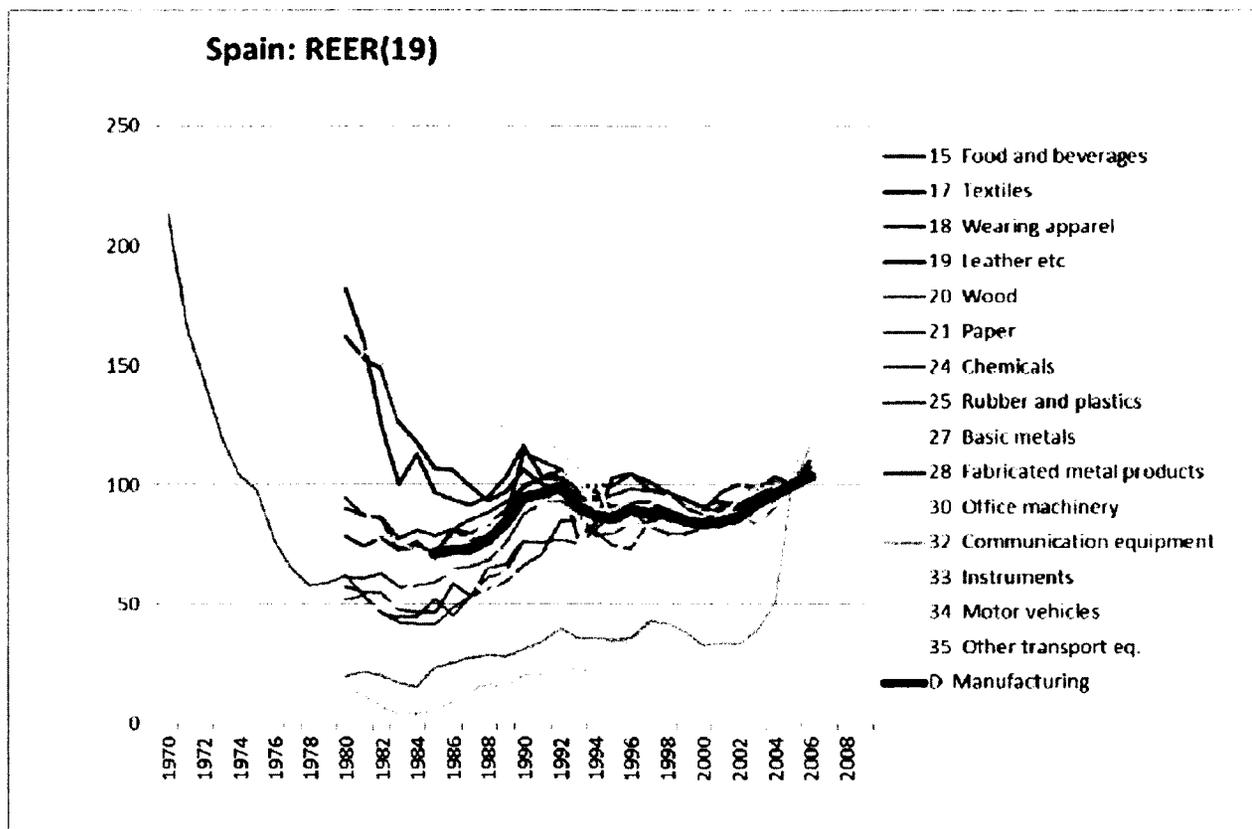
⁹ Converging countries (with initially lower incomes) observe a marked increase in prices due to the sudden productivity rate difference

ECORYS Nederland BV (2011, p. 17) undertakes a review of the usage of unit labour costs as a relevant measure in an extensive literature review, admitting that unit labour costs reflect ‘a wider economic process’ and making the case, as the European Commission (2009) did, that ‘sectoral unit labour costs are more relevant than a whole-economy measure for assessing change in competitiveness’. The European Commission (2009, p. 29) states that:

‘Since all sectors within an economy compete for workers in the same labour market, wages in each sector will reflect the average level of productivity in the economy. If there is a sector where we have a comparative advantage, we should expect wages to grow more slowly than productivity, hence lowering ULC. As a consequence, sectorial ULC may point to comparative advantages and disadvantages vis-à-vis our trade partners without looking at trade flows.’

Ca’Zorzi M. and Schnatz B. (2007, p. 21) examine empirically six alternative measures of cost/price competitiveness (including unit labour costs for the manufacturing industry and for the whole economy) in the Eurozone but they ‘do not find that any one measure outperforms the others’. As such, unit labour costs are an acceptable measure, though not a conclusive one. The sectorial divide is shown in Figure 2 and Figure 3.

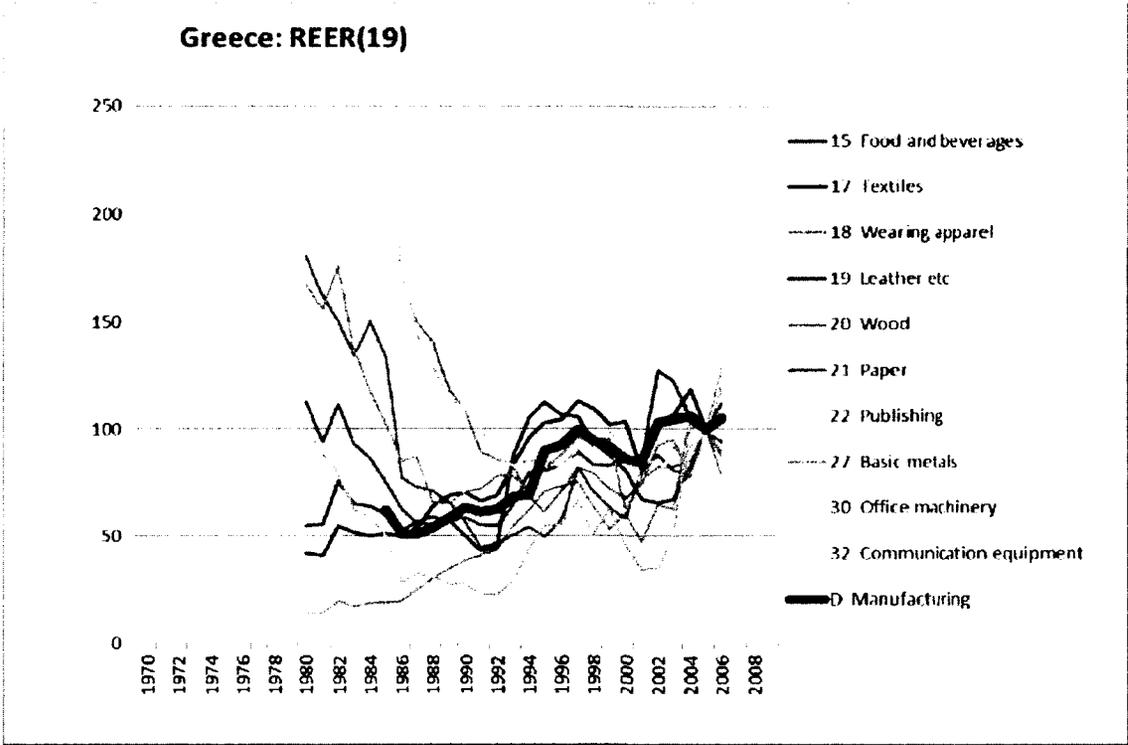
Figure 2: Unit Labour Cost by Industry Sector, Spain



Source ECORYS Nederland BV, 2011

As can be observed in Figure 2 the unit labour costs have increased in nearly all sectors of the Spanish economy. This reflects the general unit labour cost as depicted in Figure 1, showing deterioration in competitiveness.

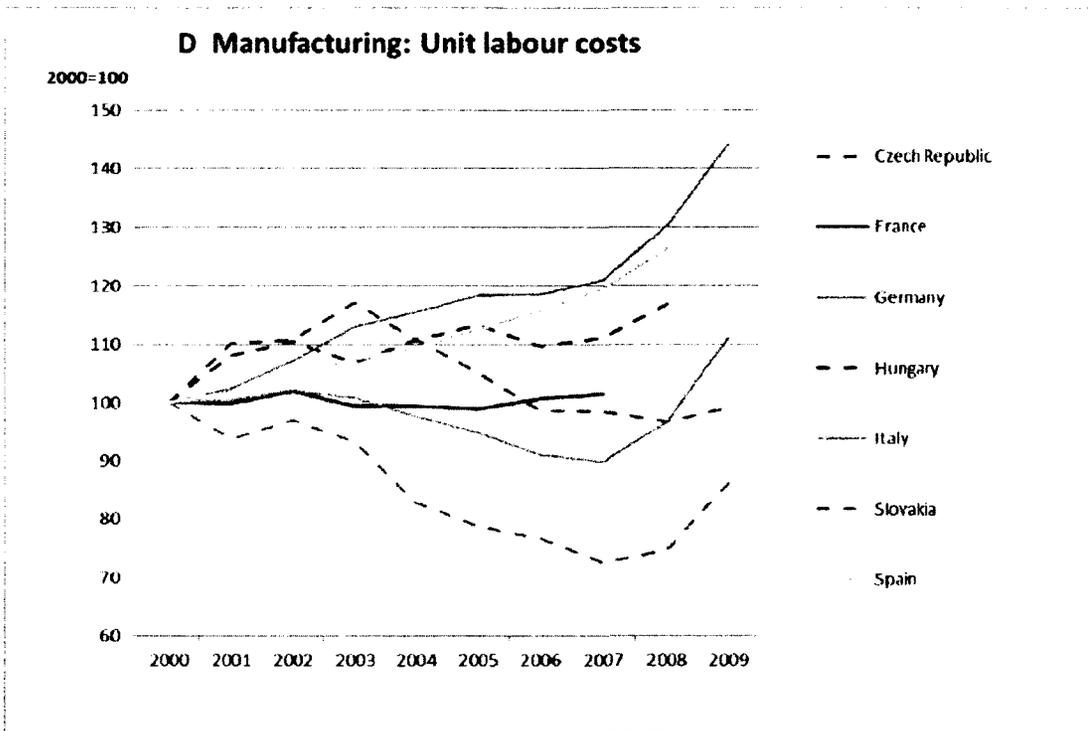
Figure 3: Unit Labour Costs by Industry Sector, Greece



Source ECORYS Nederland BV, 2011

The same pattern is observed in Greece as in Spain, as evidenced by Figure 3. We can note a general increase beginning in 1986, reaching a peak for that period in 1995, after which, a decrease is visible. The years 1995-2001 represent the period when Greece pushed to join the euro, during which time the effectuated reforms temporarily decreased the costs of labour. It can be observed that in 2002, a steep increase re-emerges, with some leveling-off in the following years, though unit labour costs remain at levels that are at their highest since transitioning to democracy.

Figure 4: Unit Labour Costs in Selected Member States



Source ECORYS Nederland BV, 2011

Slovakia, too, has seen an increase in its unit labour costs since it joined the euro in 2007 but as Figure 4 shows, unit labour costs have remained well below other member states, especially Spain and Greece.

ECORYS Nederland BV (2011, p. 21) state that it can be generally concluded that specific benefits aside, ‘small protected states gain economic and political power in entering the EU and the EMU, while the contrary goes for large ones.’

Silvia (2004) challenges the assertions of an endogenous currency area citing that, at the time of his writing, there had been no progress toward flexibility or integration of the labour markets in

the Eurozone. Instead, a ‘rigidity trap has developed in the euro area, consisting of relatively tight monetary policy, forced fiscal consolidation, and a risk of deflation in some economies’, which added to the challenge of achieving structural reforms in European labour markets (Silvia, 2004, p. 163).

Labour unions

Haffner et al. (2005) put forth the argument that competition would lead to a reduced role for unions. They argue that an ‘increase in product market competition will reduce the rewards that unions are able to extract from firms on behalf of their members’ (Haffner et al., 2005, p. 175). They use that reason to suggest that such a change could lead to a fall in union participation which would be reinforced if the fall in entry barriers to traditionally unionized sectors led to an increase in the number of new non-union firms. Haffner et al. (2005) engage two scenarios: On one hand, if increased competition means that firms would be obliged to respond more rapidly to shocks, they will press for more flexibility in employment contracts. On the other, employees may feel that they have lost job security and thus would demand increased protection. The government could also play a role by choosing to revise and reduce employment protection legislation and scale back the generosity of unemployment benefits. Tvrdon (2011) summarizes that the result would be that costs of increased flexibility will be transferred to tax payers.

Bertola (2003), however, explains that the institutional frameworks of labour markets in the EU countries are relatively stable and resistant to reforms. It is not entirely clear whether this is the result or an effect of the fact that economic integration is not yet complete within the EU which means that the advantages of labour specialization and flexibility have yet to realize their potential. Bertola explains that removing barriers is associated with social and political pressures (generally

linked with elections), which strengthen the resistance to reforms. As we will observe, labour market performances vary across EU member states, as do the integration reform pressures present in each member state. Bertola & Garibaldi (2003) pointed out that the variance in levels of economic development across EU member states explains much of Europe's heterogeneity as regards to the large variety of labour policies pursued. This view is supported by Haffner et al. (2005) who claim that the movement towards policy unification has so far not been realized.

Bentolila and Gilles (2000) explore whether the change of monetary authority will help or hinder labour market reform within the Eurozone. They disagree with the idea that increased rigidity leads to more costs associated with EMU enlargement. The main conclusions of their study are that monetary union creates the necessary incentives needed to alter an economy's structure in order to improve its response to shocks but that this may result in more rigid labour markets and that EMU reduces the incentives for a large scale reform of the labour market 'because monetary policy is very useful in order to get the best possible transition path to the new equilibrium' but there is a case to be made for the coordination of labour market structural reforms across the member states (Bentolila and Gilles, 2000, p. 32).

The first part of the Bentolila and Gilles (2000) conclusion has been proven inaccurate by many authors, including Duval & Elmeskov (2006) that found that 'the effect of EMU is only a marginal influence' and while euro area countries have taken on more extensive reforms than other OECD countries, there is little evidence that EMU facilitated the change (Duval & Elmeskov, 2006, p. 11). More importantly, they found that:

'There appears to have been a slowdown in the reform process in EMU countries after the formal advent of the euro – though this could reflect the prior race to qualify for EMU. Furthermore, EMU countries – with the exception of a few small ones – have

shown no particular ability to carry out needed reforms in areas where political resistance is normally strong (with the exception of retirement schemes where impending fiscal pressures are particularly large in EMU countries)' (Duval & Elmeskov, 2006, p. 5).

Tvrdon (2011, p. 16) confirms that 'generally speaking, labo[u]r market performance in the EU as a whole has a rigid character.'

1.1.2.1 Taxation

Within the heterogeneous cross-national policy convergence field (see Knill, 2005), the task of tax approximation is of great importance in the European integration. The EU must face the tradeoff between the national sovereignty and the single market requisites and even the ambition of a *realpolitik* union within the new scenario created after the Treaty of the European Union that can be addressed from the classical integration theory or the multi-level governance theory (Jachtenfuchs, 2001).

Delgado & Presno (2010) expanded on the notion that countries compete for mobile factors in an integrated area with free movement of goods, services, capital and labour. Since labour is less mobile than capital, the tax structure will be more based on labour income. This change would demonstrate a change of tax burden from mobile to immobile tax bases, though a caveat should be made that unemployment, amongst other factors, would serve to curb some of the increase in the labour taxation.

It is clear that Member States do not all have the same economic structure or the same public welfare system. Greece tax-to-GDP ratio is far from the EU average and is amongst the lowest in the Eurozone. In the integration of EU, the fiscal magnitudes are not the central task of the process. The harmonization rules in indirect taxation, based on minimum rates, and the slight

agreement on capital incomes approved in the last years, do not constitute a hard and unique tax policy of the Union. Moreover, the Maastricht criteria to entry in the EMU refer only to the public deficit and national debt which must be below 3% and 60% of GDP respectively.

Delgado & Presno (2010) review many works on taxation policy and their effects in order to determine whether convergence is or is not taking place. They cite Mendoza et al. (1997) who elaborated a theoretical and empirical study on the relationship between tax policy and long-run growth, and Tosun and Abizadeh (2005) that performed an empirical study of the relation between tax mix and economic growth. Wang (2007) focused on tax burden and growth, while Lee and Gordon (2005) study the influence of tax structure over economic growth with a world sample of 70 countries, leading to their findings of a negative effect of the corporate tax rate on growth.

Delgado & Presno's (2010, p.12) empirical evidence shows that as regards tax policies few convergences exist, suggesting that 'tax policies remain largely national and the vaguely designed harmonization measures and other factors such as tax competition are not equalizing the tax burden or the tax structure in the EU.' The main finding of the paper is that there has been little progress in the field of tax policy convergence in last 15 or 20 years, with the majority of convergence occurring during the 1980s and 1990s- the time immediately after Greece and Spain joined the EU, which is usually referred to as the 'catching-up period' for these countries.

Jourard (2002) provides an informative account of the tax systems in EU member states which finds that the tax burden in the EU is much higher compared to other OECD countries and that the tax mix shows that emphasis is placed on social security contributions and consumption, with corporate and property taxes representing a smaller share of tax revenue.

Trends in corporate tax rates are important in that they can suggest the direction of economic activity within a member state. Corporate tax rates can also serve to attract or discourage new investment from choosing one member state over another. Generally, the more attractive a country's corporate policies are, the more investment it will receive, boosting its overall economic activity.

According to Easson (2004) the tax that most foreign investors look for is the tax on business profits. However, whether paid directly by the enterprise or paid by employees, all taxes (personal income taxes, payroll taxes, social security contributions, consumption taxes, custom duties and import taxes) are of concern to foreign investors primarily because of their effect on labour costs. Easson (2004) argues that consumption taxes such as VAT and excise duties are of relatively little concern to foreign investors because those taxes are usually borne by the consumers.

Though Easson (2004) states that taxes in potential host countries affect considerations once the decisions to invest abroad have been made, though most econometric studies say that investors are mostly influenced in their decisions by market and political factors and that tax policy appears to have a smaller effect on the location of FDI. Nevertheless, it is fairly accepted that tax considerations do influence FDI decisions at the margin (UNCTAD, 1996). While most of the empirical studies conducted before 1990 found that taxation was a relatively minor consideration in most FDI decisions (Easson, 2004), more recent studies have suggested the opposite. According to OECD Report, *Corporate Tax Incentives for Foreign Direct Investment* (2001, p. 12), 'the results of this recent work indicate that the location of real capital by manufacturing firms is sensitive to taxation and has become more so over time'. Easson (2004) explains this change as a reaction to the elimination of trade barriers. 'As trade barriers between countries are eliminated, the remaining obstacles become more important' (Easson, 2004, p. 55).

If this is indeed a more realistic understanding of the current environment, member states will view their taxation policies as a means by which to attract FDI, and will undergo the necessary changes to make their corporate tax rates more competitive vis-à-vis their neighbours.

2 Methodology

This thesis comparatively assesses Spain, Greece, Slovenia and Slovakia from three different perspectives. These perspectives, or variables, were chosen because, though not exhaustive, taken together they offer an interesting perspective on the chemistry of reform. The three variables are political influences, labour and taxation policies. The rationale for each of these variables is explained below in detail.

The first analysis covers the political situation in each country. Since every country chosen had an extended period of totalitarian rule, either fascism or communism, which marked their economic development and influenced their developmental trajectory, that destructive period is addressed first. It is covered in an overview at the beginning of each political section. The political direction of a country is important as it sets the course for the country. Changes to the social, economic, legal and cultural landscapes can be made, and often are, by the political party in power. The evolution of political power is also important as it reflects the changing dynamics and attitudes of the citizens.

The labour market figures as the second variable examined on the road to the euro. The labour market was chosen because the flexibility and adaptability of the labour market heavily influences a country's transition. It also impacts the development and modernization of a country. In an economy that is open, where labour contracts are flexible and information is easily and readily available, labour markets can serve to facilitate the most effective use of resources, both capital and human. If workers can freely move between jobs and sectors, have the ability to progress in their field or re-train in order to obtain a better position, the likelihood that the worker will be productive is increased. In a situation, however, where the labour market rigidities disincentive the worker

from pursuing work opportunities or makes it very hard and costly for a company to hire and fire employees, productivity stagnates. Where this is the case, international investment also is limited. Companies want to be assured that if they invest in a country they will have access to trained personnel, and will be able to hire and fire them as their business needs change.

In countries where labour unions are very powerful their influence can represent either a betterment of working conditions or a degradation of productivity, depending on how the unions see their role in society and vis-à-vis the companies and the government. If the unions choose to use their platform to represent workers so that their working conditions are improved and their pay is reflective of their work quality, then the labour market benefits in the long run. The opposite can also exist, where strong unions take the labour market hostage, leading to economic paralysis with long-reaching consequences. It is important that unions distinguish action for the sake of it from action for a purpose. Reflection must be given on how much protection labour needs in a democratic, developed nation where the third sector¹⁰ is strong and legislation ensures that minimum thresholds are more than sufficient.

A rigid labour market, where new entrants cannot find suitable jobs and existing labourers are inefficient but unwilling to leave their position, can create structural problems. One pertinent and troublesome problem is high long-term unemployment. This is an issue in the greater sense because frustrated citizens that cannot find employment will leave the country in search for better opportunities in other labour markets. While this is an acceptable solution at the micro level, at the

¹⁰ The third sector, also known as the civic sector, refers to voluntary, not-for-profit social activities. The first sector refers to government and the related services provided; the second sector refers to the private or business sector.

macro level, this can affect a country in the long-run. This problem also demotivates the labour force, which can be linked to reduced productivity.

Also important is the social security support for those that are unemployed. Unemployment insurance must be devised in a way that does not discourage workers from seeking employment. Some countries have very generous provisions for unemployment insurance and lax rules about monitoring a worker's attempts at finding employment. This can create a situation whereby a worker will choose to stay unemployed for an extended period of time, longer than s/he normally would have done, because the benefits of unemployment are sufficient to encourage this action. This is a serious problem, not least because the longer a worker is out of the workforce, the harder it is to re-integrate and the longer it is until that worker becomes productive again.

The pension system also falls under the labour market. How a pension system is derived differs from country to country but the concept and principle remains constant. A pension system is necessary so that, upon retirement, workers that have contributed to making the economy productive during their lifetimes can retire and be able to subsist and even maintain a similar level of lifestyle. Pensions, though, must be sustained by ensuring that the amount of active labourers in the economy is greater than the amount of retirees. If this is not met, it becomes impossible for the country to maintain a fair and equitable pension system as funding is not sufficient to cover the operating costs. Depending on the provisions of the pension plan, be it too generous or too stringent, pensions may incentivize or dis-incentivize workers from retiring when they should. If people do not feel that retirement is an economically viable option, they will stay in the workforce, even if their personal productivity has declined. This hurts the labour market because not only are new, young workers not able to enter the labour force, but the overall efficiency and effectiveness of the labour market decreases, hurting productivity and the competitiveness of the country overall.

Taxation is the third variable in the analysis. Taxation is essential to an economy. It provides the majority of the public budget. Be it through personal income tax, corporate income tax, taxes levied on investment and trade, or indirect tax, taxation is a central pillar of any economy.

The tax code and its application can have a pronounced impact on the performance of a country and its ability to manage its economy. Not only is the structure important, but the enforcement is also key. No matter what the tax structure and corresponding laws are, if professionals are not trained well or are not fairly remunerated, problems will persist including tax evasion, low tax morale and tax fraud.

Which taxes are emphasized also matters. A very high income tax, while creating revenue, may be met with serious hostility if the citizens do not believe that they are seeing the positive effects in such domains as social services or education. Corporate tax rates are equally important as they drive business to or from a country. Any enterprise must be able to imagine a viable and profitable future for itself, in an environment where, if managed properly, its business can grow and profits can increase. If this seems unlikely because of the regulatory nature of a country, the business will choose to leave and pursue commerce in a different country.

The variables were chosen for many reasons. Labour market flexibility is essential to creating a workforce that is mobile and adaptive to changing economic environments. A strong labour market contributes to financing government activity and thus has an impact upon the government's ability to provide public goods and services to its citizens and maintain a robust economy.

If the political powers create an environment where they work with the unions to establish a fair but competitive labour market, and devise a taxation system that allows the government to collect enough revenue to cover its costs and maintain a modernized economy, then citizens will be

willing to work and contribute to productivity because they can identify the benefits of the taxes they are paying reflected in the social services they are entitled to. Similarly, if businesses believe that they have access to a well-trained labour market that is willing to be productive, in a country where the government develops and enforces a tax system that encourages business but does not penalize workers, then they will be willing to increase their investment, thus contributing to the betterment of that country.

The labour market and taxation system must also be perceived as having the need for periodic review. The political forces must understand that as times change and industries rise and fall in importance, the labour market laws and regulations alongside the taxation system and its burden on the tax base have to be flexible enough to adapt to changing circumstances. One example is the change in retirement age. As life expectancy increases, people are both able to work longer and likely to live on longer after retirement. As a result, they will require more money set aside for their retirement. In order to address this, there needs to be an increase in that individual's time worked, and therefore his/her pension contribution, in order to cover the added costs.

The time period chosen for analysis varies in length for each member state, but represents the same phase for all of the countries. The analysis begins at the time of their transition from dictatorships to democracies and covers the period of their euro adoption. This time is important because it represents the phase during which the most reforms were needed in order to qualify for the euro. As the criteria for the euro was rigorous, member states needed to undergo certain reforms to satisfy the convergence criteria. The reforms chosen and their implementation are assessed in the case studies below.

3 Case Studies

3.1 Spain

Overview

The Spanish civil war, launched by a military coup waged by the Nationalists against the Republican government, began in 1936 and ended in 1939 with the victory of the extreme right-wing General Francisco Franco. By the end of the Spanish civil war, Franco had been proclaimed the *Generalísimo* (supreme military leader) of the national army and the head of state (*Jefe de Estado*). Following the end of World War II, in which Spain did not participate, Franco consolidated power and was formally recognized as the head of the Spanish state¹¹ by foreign states (Carr, 1982).

In 1947, Franco passed a referendum making Spain a monarchy to be headed by him for life. In 1969, he proclaimed that Prince Juan Carlos was to be his successor. Franco's Spain was inward looking, highly protected and dominated by the agricultural sector. Social provisions were weak (reflecting the very right-wing doctrine prescribed by Franco) and the third sector was virtually inexistent. With the death of Franco in 1975, the monarchy was restored and Prince Juan Carlos became the head of state. Within three years, Prince Juan Carlos reintroduced democracy in Spain, establishing the country as a parliamentary constitutional monarchy. Extensive reforms were launched in order to rectify the damage caused by 35 years of dictatorial rule. As elaborated by Koch (2004, p. 17), Spain needed to transform a 'protected and inwardly focused economy into an

¹¹ Britain and France recognized Franco as the head of the Spanish state in February 1945; the United States had recognized him in 1939 (Palmer, 1996).

open and competitive one'. Spain was also in dire need of institutions that could develop, strengthen and regulate the labour market. The modern Spanish state had to transition quickly and peacefully to a democracy and had to act swiftly to lessen the economic depression through modernization.

3.1.1 Political Forces

1970s

In 1976, the Spanish parliament, known as the *Cortes*, passed the *Ley para la Reforma Política*¹² (Law for Political Reform), which officially dissolved the Franco-era system and established the parliamentary democracy and paved the way for the first elections. The first post-Franco democratic elections were held in June 1977 (Closa & Heywood, 2004). The Unión de Centro Democrático (UCD) won the elections and Adolfo Suárez became the first democratically elected prime minister of post-dictatorship Spain. The following two years are largely viewed as transition years with the government beginning to address reform.

During the 1976-78 transition, reformist economists in Spain rejected dirigisme politics¹³ and stepped into key roles in order to control the wage-price spiral which followed the end of the Franco regime. The strategy involved two steps (Perez, 2004): First, a change was effectuated in the institutional basis of economic policy to allow the central bank more control over monetary aggregates by dismantling dirigisme regulation of the financial system as devised under the Franco

¹² Original language text available here: http://www.boe.es/aeboe/consultas/bases_datos/doc.php?id=BOE-A-1977-165

¹³ Dirigiste policies or dirigisme refers to government control or intervention, especially in business activity or the economy

regime and; secondly, the government negotiated income policies with the *Moncloa Pacts*¹⁴. Particularly, these income policies were crucial in achieving disinflation by the post-transition governments.

The UCD government began quickly to chart a course towards the European Union, then known as the European Community (EC). In July 1977, the government applied for EC membership (Closa & Heywood, 2004) and in 1979 negotiations on EC membership treaties began. Spain became a member of the European Coal and Steel Community (ECSC), the European Economic Community (EEC) and Euroatom.

Monetary and fiscal policy reforms were also launched. The UCD sought to increase government revenues in order to reduce budgetary deficits. With this objective in mind, the government began an extensive period of reform of the tax system (discussed in detail in the tax section) which led to an increase in income and heritage taxes in 1977 (Comín, 2007) and the first reform of the personal income tax (PIT) in 1978 (Martínez-Vázquez & Sanz-Sanz, 2007). A telling snapshot of the tax reform begun by the UCD government is that in 1975, tax revenues as a percentage of Gross Domestic Product (GDP) were less than 20%. Comparatively, the OECD average for the same period was 31% of GDP (OECD, 2009). By 2002, Spain had converged with the OECD average with total tax revenues representing over 25% of GDP (Martínez-Vázquez & Sanz-Sanz, 2007). The UCD government commenced the reform of labour relationships in 1977 and introduced four main pieces of legislation (discussed in detail in the Labour section).

Tax reform began to lose support after the 1979 elections, as the weak UCD government faced opposition from both political groups and social organizations.

¹⁴ Full text available at: <http://vespito.net/historia/transi/pactos.html>

1980s

The right-wing party Alianza Popular (AP) and the business organization Confederación Española de Organizaciones Empresariales (CEOE) (Spanish Confederation of Employers' Organizations) took advantage of the UCD's weakness (a deterioration witnessed almost immediately after the Moncloa Pacts were agreed) and became increasingly critical of the government, especially the tax reforms. Prime Minister Suárez resigned in January 1981 as he, his government and the UCD as a political party faced problems on almost all fronts (Aza, 2000): the Church, the armed forces, terrorism, the Autonomous Community (regional governments) and, perhaps most importantly, the economy.

Elections were held in 1982 which saw the formation of the first Partido Socialista Obrero Español (PSOE) (Spanish Socialist Workers' Party) government, led by Felipe González (PSOE, 2006).

During their first mandate, 1982-1986, the PSOE government raised interest rates (Smith, 1998), devalued the *peseta* by 8% (Navarro, 1997), increased income tax (Smith, 1998) in an attempt to reduce public deficit, relaxed the regulation concerning foreign direct investment (FDI) and, in keeping with the PSOE's 'European goal' continued and finalized the negotiations of the EC membership treaties.

The second PSOE mandate, 1986-1989, was concentrated on applying the provisions laid out in the membership treaties and the Single European Act (SEA) as well as pursuing structural change mechanisms (SCM¹⁵s) throughout all sectors of the economy.

¹⁵ Broadly, the term refers to the processes and tools employed through which major changes are carried out in an economy. Specifically, can refer to the transfer of resources from one industry to another or the more general shift of economic organization.

The PSOE pursued an unprecedented austerity program, cutting inflation from 14% in 1982 to 4.8% in 1988 and decreasing public deficit from 5.2% in 1982 to 2.6% in 1989 (Perez, Monetary Integration and a social model in Spain, 2004). These victories were not without setbacks-unemployment reached 22% in 1985 (EL PAÍS, 1986) meaning that one in five workers at the time was unemployed. Unemployment declined only slightly with the entry of Spain into the EC in 1986 (Instituto Nacional de Estadística (INE), 2011).

In 1987, the Bank of Spain began increasing the interest rate aggressively and set out to turn the *peseta* into a 'strong' currency by keeping it within the narrow ERM central parities, a move which it hoped would also lead to disinflation (Perez, Monetary Integration and a social model in Spain, 2004). Price stability as reflected by inflation was brought down from 30% in 1977 to 15% in 1978 and 4.8% in 1988, while the budgetary deficit was curbed at 6% during the same period (Perez, Monetary Integration and a social model in Spain, 2004). Unemployment followed an inverse trajectory from that of inflation and deficits, increasing from 5% in 1976 to 22% in 1985 and remaining above 16% through the end of the 1980s (Pampillón, 2008). At the end of the decade, as unions became more aggressive in their wage demands, the government responded by advancing the *peseta*'s entry into ERM in July 1989, ahead of its 1990 schedule (Rodríguez López, 2005). The reforms and persistence of restrictive policy led to currency stabilization, decrease in inflation, decreased balance of trade (BT), current account balance, and a lower central government budget deficit which served to justify entry of *peseta* into European Monetary system in 1989 (Navarro, 1997).

1990s

The PSOE was resolved to see Spain included alongside the other EU member states in the first wave of euro adoption. To achieve inclusion, the socialist government drew up the 1992 Decree:

Plan for Economic Convergence¹⁶. The Plan consisted of three macro-economic objectives: 1. Faster economic growth, 2. Reduced trade deficit and, 3. Decreased public sector borrowing. The Plan reflected a need for urgent budgetary measures. To achieve the goals, focus was put on economic deregulation, labour market reforms, and tax reforms.

Powering through with reforms, the PSOE adopted a new stabilization program in 1993 that had 4 specific objectives (Diamandouros & Gunther, 2001). The first was to decrease inflation by half through restrictive monetary policy and limiting salary increases. The second centred on reabsorbing the balance of trade (BT) by devaluating peseta by 8%, improving competitiveness of companies and providing support to exports. The third attacked the state budget deficit through spending controls and 20% increase in income tax. The fourth objective was to re-establish growth by pursuing a policy of investment promotion.

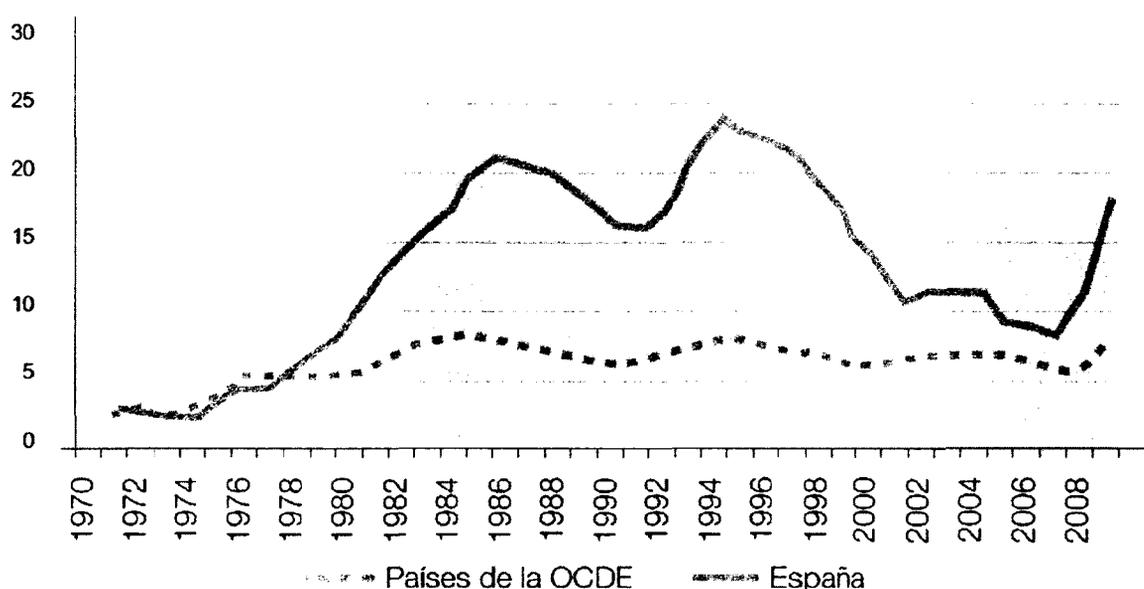
In tandem with the stabilization plan, a structural reform plan was also devised that addressed, among others, declining industries, inflexible labour market, the need to liberalize financial sector and to reform the social security sectors (Gunther, Montero, & Botella, 2004). With all the focus on austerity and growth as an afterthought, it is perhaps not surprising that in 1994, the rate of unemployment reached 25% (Perez, Monetary Integration and a social model in Spain, 2004).

González proceeded with the implementation of Maastricht convergence measures evidenced through large budgetary cuts and restrictive monetary policies in 1994 and 1995. At the time of PSOE electoral defeat in 1996, Spain was farther along the road to satisfying the fiscal and monetary criteria than many other EU member states (Jiménez, 2004). The conservative Partido

¹⁶ Royal Decree Law 5/1992 of July 21, 1992

Popular (PP) reclaimed power in the elections and completed the majority of the work left on the fiscal and monetary side, but incurred large costs as well- that of having the highest unemployment rate among the member states (Encarnación, 2008). Figure 5 depicts the unemployment rate in Spain and the OECD from 1970 to 2008. We can see that the PP government inherited a high unemployment rate at the time of their electoral success in 1996, well above 20%. In the subsequent years, unemployment decreased, however, rates remained high until near the end of the decade.

Figure 5: Unemployment Rate, Spain VS OECD, 1970-2008



Fuente: OCDE. *Labour Force Statistics*. Áreas en gris representan gobiernos del PSOE

Note: The gray-shaded areas of the graph represent PSOE governments and the white area post 1996 represents the PP government.

Source: OECD 2009

Spain looked towards monetary integration to provide the context necessary to control wages as the governments' efforts to impose wage restraint with the unions or to establish an income policy process failed.

Spain defied many predictions when it joined EMU in 1999 as it had been accepted into the EC much later than most other Member States. Perez (2004) has pointed out that despite criticism from foreign press, Spain, at the end of 1997, was actually much closer to meeting the convergence criteria set out in the Maastricht Treaty than Italy (and, almost incredulously, than both Belgium and Germany). This apparent compliance was not without costs- manifesting most painfully through the high unemployment by now a staple in Spain's macroeconomic performance.

The entry into EMU brought with it many changes. Fast economic growth and recovery was seen in the Spanish labour market and unemployment fell from a staggering 22% in 1996 to 14.5% in the first half of 2000. The public deficit was reduced to a remarkable 1% of GDP in 1999.

2000 onwards

The PP government used this new-found fiscal breathing space to reduce the taxes on both personal and corporate income. The government also upheld the Stability and Growth Pact (SGP) objective of a balanced budget by 2001 by way of increasing the primary budgetary expenditure cuts.

As the SGP has limits placed on a government's ability to augment social spending, funding was not increased in order to address unemployment which can perhaps be seen as one of the social compromises of partaking in EMU (Perez, Monetary Integration and a social model in Spain, 2004). Basically, the governments of the EMU member states placed a ceiling on non-wage labour costs in efforts to maintain competitiveness within the Eurozone, a principle that was accepted by all parties.

3.1.2 Structural Labour Reforms

With the transition to democracy, Spain engaged in a reform of the labour dimension. The *Moncloa Pacts*, signed by all labour market participants- businesses, unions and the government, set out to define the new industrial relations setting that would restrain wage demands, control inflation foster business, and contain labour militancy (Koch, 2004). The development of the institutions of labour market and welfare regulation in Spain coincided with the crisis near the end of the 1970s, whose main feature was a high level of unemployment (Koch, 2004). For reforms to be successful, they had to address the segregated labour market that was split between those with permanent contracts and consequently job security and effective labour union representation and those who were excluded from the labour market. The latter group was mainly comprised of young workers who found it hard to join the formal economy because of the long-term fixed contracts and high costs of dismissal faced by employers. Young workers were kept on temporary contracts whose provisions made them vulnerable to firing without much notice.

Labour Unions

The two major labour unions (Callejo, Meseguer, & Moron, 2008) in Spain are the Communist-dominated *Comisiones Obreras* (Workers Commissions) (CCOO) and the Socialist General Union of Workers (UGT). There are various smaller unions representing the regional interests of each of Spain's 17 autonomous regions, but focus will concentrate on the CCOO and the UGT as they are national unions. These two unions regained power and status after the death of Franco and with the re-establishment of democracy.

Royal Decree 17¹⁷ of March 1977 introduced the right to strike into legislation and also softened the restrictions on firing which were left over from the Franco era. The following month, the government issued Royal Decree 19 (Ley 19/1977¹⁸), a law on trade unions which granted them the freedom of association.

March 1980 saw the introduction of the *Ley 8/1980, del Estatutos de Los Trabajadores*¹⁹ (ELT). The ELT is the Workers' Statute, a framework law outlining the rights and responsibilities of workers in Spain. The statute also outlines the format for collective bargaining, recognizing the right of the elected representatives of the workers to negotiate on their behalf.

In October 1980, the UCD government passed *Ley 51/1980, Básica de Empleo*²⁰ (Basic law on employment). Here, guarantees pertaining to a minimum wage and social security were specified. Consultation between the government and the labour unions grew and was reinforced during this time but the growing effects of the crisis (set off by the second oil crisis in 1979) weakened the unions' bargaining position. A class perspective retreated in the face of individualism and/or corporatism of labour action that focused on immediate and limited demands (Vega Garcia & Perez, 2000). Increasingly, unions became dependent on state subsidies that were used as rewards

¹⁷ Full text, in Spanish, can be accessed here : <http://www.cgt.es/ssm/Textos%20Legales/RD1%2017%20Huelga.pdf>

¹⁸ Full text, in Spanish, can be accessed here: http://www.boe.es/aeboe/consultas/bases_datos/doc.php?id=BOE-A-1977-10562

¹⁹ Full text, in Spanish, can be accessed here: http://www.boe.es/aeboe/consultas/bases_datos/doc.php?id=BOE-A-1980-5683

²⁰ Full text, in Spanish, can be accessed here: <http://sede.juntaex.es/tramitedoc/b7e3d098-1955-458b-ad6d-bfa1aa8cf98f/LeyEST51-80.pdf>

for departing from ideologically radical stances. The persistence of the crisis distanced unions from their role in the workforce and by the mid-1990s they had re-assessed their ‘confrontational strategies’, concentrating instead on bringing about a political context that provided opportunities for bargaining at the national level (Koch, 2004, p. 26). The unions accepted increased flexibility and wage moderation in return for greater employment stability and social benefits.

Two labour reforms took place in the 1990s, first in 1994 and then in 1997. The *Reforma Laboural de 1994*, taken on by the PSOE government, was adopted despite the objections of the unions but with the support of Spanish business organizations anxious to gain greater internal flexibility in the run-up to European market integration (Tompson & Price, 2009). The stated aim of the government was to use the reforms to rein in inflation and bring down public-sector deficits in order to qualify for the first-wave of EMU (Tompson & Price, 2009). The reform saw the amendment of many of the precepts of the major labour laws including the *Worker’s Statute*, the *Labour Procedure Act* and the *Labour Offences and Sanctions Act*. It included the adoption of a number of new acts and the revision of numerous legislations on special working hours, temporary/fixed-term contracts, training contracts and redundancy procedures. The major aspects of the reform were the following: 1) a significant transfer of regulatory powers regarding pay and conditions from the law to collective agreements; 2) the decentralization of collective bargaining, especially in the form of enterprise agreements; 3) a lifting of the public monopoly of job placement, to allow the operation of private employment agencies and temporary employment agencies; 4) facilitation of internal labour mobility within the enterprise; 5) reduction of the costs of individual dismissal, through a restriction of the cases in which back pay awarded after dismissal appeal hearings is payable by employers; and 6) a modest relaxation of the rules governing collective dismissal/redundancy (Eurofund, 2009).

The 1997 reform was undertaken by the newly-elected PP government. The PP had made unemployment a major issue of their campaign and had promised to pursue deeper labour market reforms if elected but had not specified what those reforms would entail (El Mundo, 1997). In fact, the PP had stressed that whatever the reforms, they had the utmost intention to negotiate them with social partners, in attempts, as pointed out by Thompson and Price (2009), to assuage fears of those on the left about the coming of a right-wing party. The unions, having been marginalized in the 1994 reforms welcomed the olive branch and after 10 months of talks, signed the *Reales Decretos Leyes 8/1997* and *9/1997* based on the *Pacto Laboural por el Empleo* (Labour Agreement for Employment), a three-part agreement. The first part of the agreement dealt with employment stability, the second with collective bargaining, and the third with the regulation of working conditions for those sectors that the 1994 reform had overlooked.

In return, the unions received some concessions, including stricter conditions on the use of temporary contracts, a return to the pre-1994-reform where national sectorial agreements set sectorial minimum wages and defined overall wage structures and a transition to the 35-hour work week (Tompson & Price, 2009). As regards the implementation, the collective bargaining reform proved the most difficult and made only limited headway, largely because of resistance from within both the trade union movement and the employers' organizations (Tompson & Price, 2009).

The PP pursued reforms again in 2001. The unions' attitude at the time of this reform had turned more hostile because they viewed that the government had 'gone back on a promise not to use its parliamentary majority to bypass the unions and the opposition' (Tompson & Price, 2009, p. 323). The PP government insisted that wage demands had to be 'moderate and only slightly above the expected rate of inflation' (Koch, 2004, p. 94). The government, UGT and CCOO, and the employer's organization CEOE reached agreement (Koch, 2004) with the only concession being

that compensation for dismissal of temporary workers amounted to 8 days' pay for every year worked (Tompson & Price, 2009).

Laparra and Garcia (2003) found that, following the 1997 and 2001 reforms, possibilities for the unemployed of finding any job have significantly improved, with the chance of finding a permanent job increasing for both unemployed and temporary workers -especially for the former.

Figure 5 (shown earlier) shows that unemployment did respond to the labour reforms. A decrease can be observed commencing in 1996, coinciding with the PSOE's electoral defeat and the beginning of the PP era. As discussed above, the PP campaigning extensively on labour market reforms, and their policies and rapprochement to the unions, including social partners, appear to have paid off. Indeed, in 2001, the unemployment rate reached almost 10%, a significant decrease from earlier periods. Although the unemployment rate has never been as low as it was at the time of transition, about 5%, we can see a real decrease until the September 2001 terrorist attacks. After 9/11, unemployment began to increase again, leveling off until 2005 and decreasing slightly between 2005 and 2007. In 2008 a marked increase can be observed. Though the date coincides with the beginning of the Lehman saga and ensuing credit crisis in the United States, the date is before the current credit-turned economic crisis began in Europe and so the marked increase is somewhat puzzling. Further research as to the culminating factors that led to such an abrupt increase would add to this field.

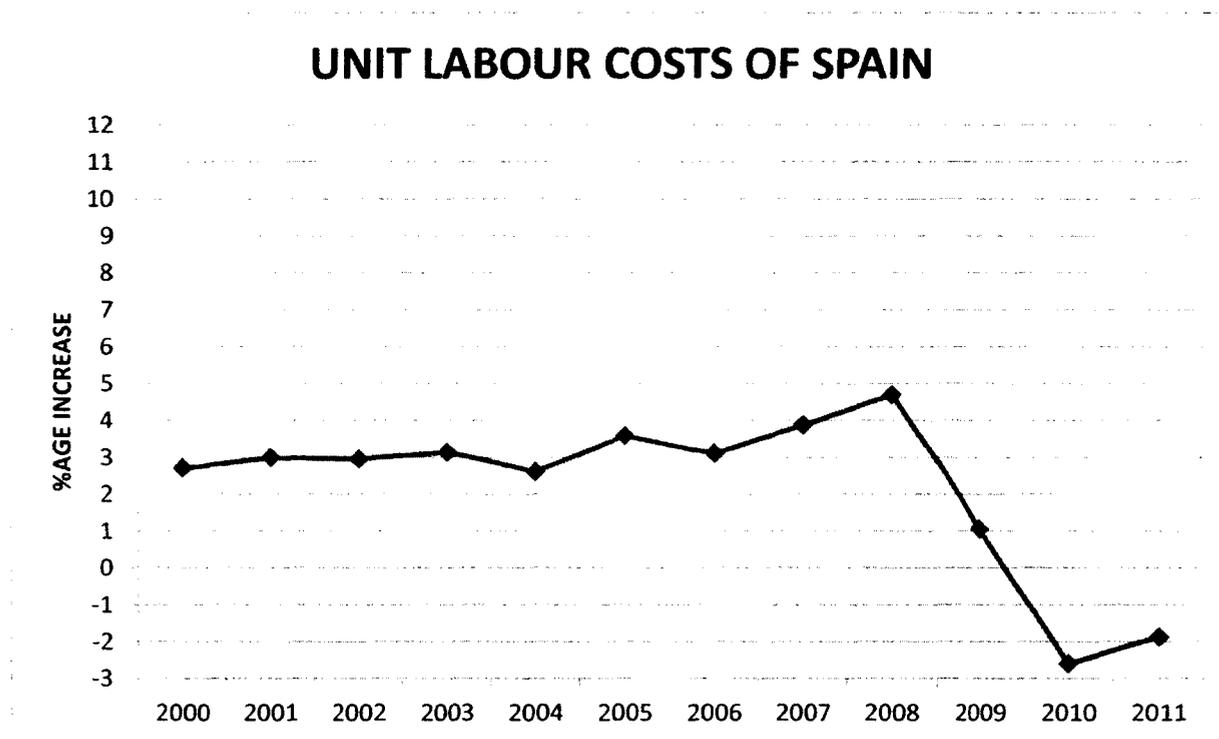
Unemployment benefits are quite generous and segregated by sector, in an effort to target benefits to workers most affected by cyclical changes. Spain was very cautious not to introduce reforms to benefits when addressing overall labour reforms (Dyson, et al., 2002).

When Spain joined the EC its labour costs were seen as a competitive advantage which attracted international investment. The lower relative labour costs were in large part the result of the Moncloa Pacts whose reforms had lowered labour costs and encouraged job creation in both the private and public sectors (Navarro, 1997). Throughout the 1980s and 1990s, the increased use of short-term contracts and the reduced costs for termination of employment added to the creation of a labour environment where unemployed increased while salaries declined (Navarro, 1997).

Figure 6 depicts the unit labour costs (ULC) in Spain following their adoption of the euro. We can note a steady slight increase in labour costs until 2003, after which we note a stronger increase until 2008, which coincides with the onset of the global financial crises. This reflects that Spain was able to keep its ULCs low before the euro adoption as it had unrestricted access to monetary policy and could devalue its national currency as needed. Figure 7 expands on the ULCs increase in Spain by sector. There we observe a marked and steady increase across all sectors of the economy. It is important to note that Figure 7 covers industry ULCs until 2008, which we know from Figure 6 to be the end of the increases in ULCs. Olsen (2012) conducted a study of the Spanish labour market vis-à-vis the German market and concluded that ULCs from 2000-2008 increased in Spain by 32%, while they remained constant in Germany. Conducting analysis on productivity in Spain, Olsen (2012) shows that the ULC increases were not the result of productivity increases in Spain versus Germany, and in fact notes that productivity increases have lagged behind wage increases in Spain. As Spain and Germany share a common currency since 1999, this has made Spain relatively less competitive. While in absolute terms, paying for an hour of work in Germany is more expensive than in Spain, those same costs have increased by 44% from 2000 to 2009 in Spain, while in Germany that figure is 16% (Olsen, 2012). In part, this is a result of Spain's catching up process with European standards. However, it is also indicative of

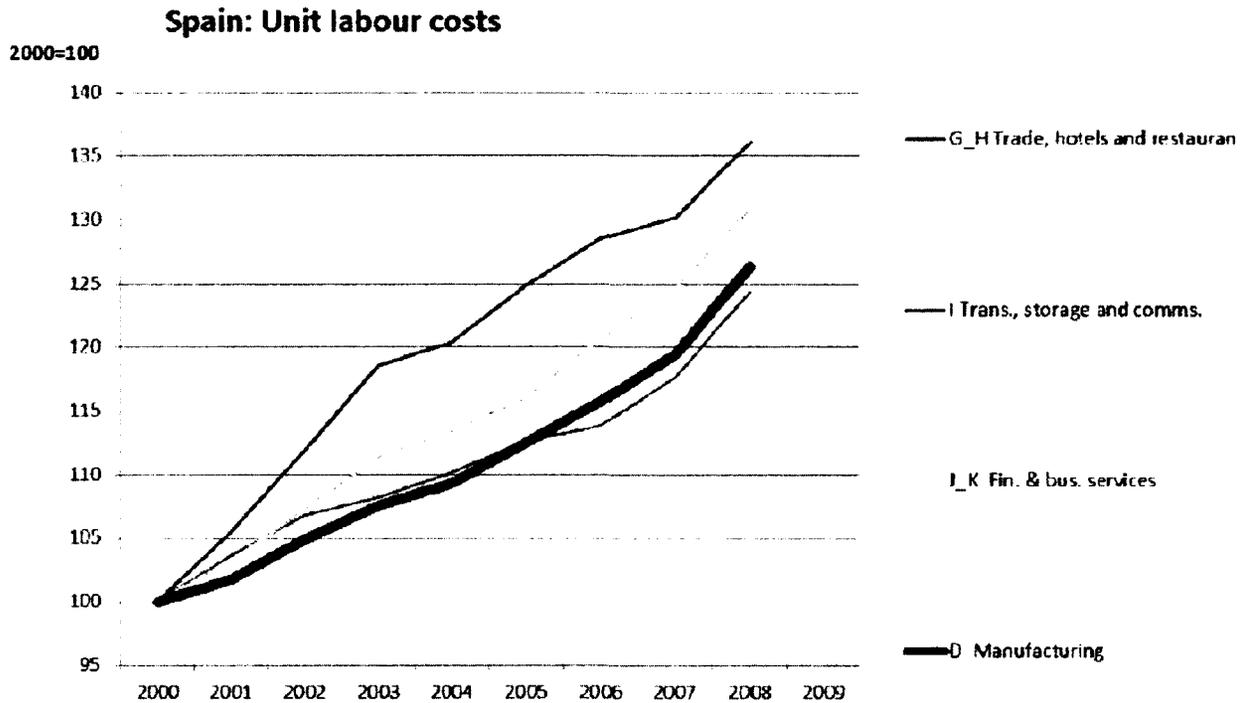
structural problems within the Spanish labour market that have led to decreasing productivity but higher wages.

Figure 6: Unit Labour Cost Spain, 2000-2011



Source OECD data 2012

Figure 7 : Spanish Unit Labour Costs Per Industry, 2000-2008



Source ECORYS (2011)

Pensions

The most significant changes in Spain were the 1997 and the 2002 pension reforms.

The 1997 reform, undertaken by the PP, established a pay-as-you-go (PAYG) system (Bonin et al., 1999). This reform, though necessary, did not go far enough to ensure long-term sustainability and was criticized soon after it came into effect. The tax-benefit linkage needed to be addressed as did an increase in the retirement age (Bonin et al., 1999).

The 2002 reform sought to address the issue of sustainability. This was done through an increase to the number of years in the workforce necessary before retirement (from 8 to 15), an increase in the

penalties for early retirement and a re-assessment of the eligibility conditions for old-age pensions (Bonin et al., 1999). While the average years worked was increased, the eligibility conditions were relaxed, so the overall benefit for the system's sustainability was not maximized. In analyzing these changes, Martin and Marcos (2010) concluded that the Spanish pension system is unsustainable and that the reforms undertaken were not effective in improving the system's sustainability.

Most recently, the current PP government has begun extensive reforms, including widely unpopular pension reforms. The first measures passed will raise the statutory retirement age from 65 to 67 between 2013 and 2027, increase the number of years to calculate the earnings base from 15 years to 25 and increase contribution years for the full pension from 35 years to 38.5 (Sourbes, 2011). The latest measure aims at redefining pensioners' benefits and has been met with criticism from the country's labour unions and opposition politicians.

3.1.3 Tax reform

The Franco regime had favoured the middle and upper classes through a tax system that exercised a low tax burden and a highly regressive sales tax²¹, but no income tax or tax on wealth (Clark, 1979). This in turn bred a culture of citizens and business owners that were very reluctant to tax modernization. The consolidation of the welfare state (a consequence of the Moncloa Pacts) demanded increased tax revenue and social insurance contributions in order to finance the new budgetary functions. Fiscal fraud was prevalent and generally, the more an individual earned, the more likely s/he was to try to evade paying taxes (Martínez-Vázquez & Sanz-Sanz, 2007).

²¹ Sales taxes on staple items like flour and salt made up 10-12% of the total tax burden.

Martínez-Vázquez & Sanz-Sanz, (2007) argue that Franco was not interested in fighting fiscal fraud. First, fraud was not considered a criminal offence, it was only dealt with administratively; second, bank secrecy on current accounts was sanctioned; third, there was a ban on publishing tax payer lists and, fourth, the Ministers of Finance kept a deficient tax system, in that it was poorly endowed with personnel and resources.

Evidently, the Franco-era tax system had negative effects on the development of the national economy. The deficit produced by the lack of tax revenue did not provide enough resources for the State to provide the public goods and services required to industrialize the economy (Martínez-Vázquez & Sanz-Sanz, 2007). Needless to say, it also hampered social stability as it did not contribute to income redistribution, favouring instead the income inequality devised by the unfair tax burden.

The transition government of the UCD included in the Moncloa Pacts a section on tax reforms but with the signing of the Constitution in 1978, tax reforms were delayed and stretched out in time. Tax reforms lost support after the 1979 elections because of the weakness of the UCD government. Indeed, the UCD was not able to correct the initial defects of the reform, nor was it able to strengthen the Tax Administration or map out a cohesive and decisive future for when reform might be implemented.

The UCD government did manage to introduce four tax laws. The first democratically passed law in Spain was *Ley 50/1977*, the Law of Urgent Tax Reforms Measures, passed on November 14, 1977, which declared tax fraud a crime, removed the banker's duty of secrecy and established a wealth tax, amongst other things. *Ley 44 & 61/1978* on Personal Income Tax and Corporate Income Tax, respectively, were introduced the following year. Two laws, *Ley 30/1979* and *Law*

32/1980 also dealt with special taxes and taxes on capital transfers. These reforms were met with very little public criticism, including businesses and lobbies, although they did try to delay the legislation from passing in the *Cortes* (Martínez-Vázquez & Sanz-Sanz, 2007). As a result, only the corporate tax and capital transfers bills passed, while the value-added-tax (VAT) was postponed.

Following their 1982 electoral victory, the PSOE government began to deliver on the campaign promise of tax reform. The socialist government moved quickly to complete the tax system that had been outlined in the Moncloa Pacts. The same day that Spain joined the EEC, January 1, 1986, the VAT became effective. The VAT, a necessary condition for entry into EEC, replaced a number of existing indirect taxes. Progressivity was also pursued via a partial reform of the personal income tax (Martínez-Vázquez & Sanz-Sanz, 2007). Further laws were introduced in order to fight tax fraud and evasion. The tax harmonization with the EEC (via the VAT) increased excise taxes, which had previously been lower in Spain than the rest of Europe (Comin, 2006). Spain had to adjust itself very quickly to the European fiscal trends and norms which, in turn, required adjustments to the tax system.

In 1991, Spain adopted corporate income tax at the European Community standards. The individual income tax was also harmonized.

The system was then left alone until the PP was elected in 1996, having had promised voters tax reductions in the electoral run-up. Spain during this time was aligning itself very closely to its European neighbours and was preparing for the first wave of EMU. As a result, the main measures

carried out by the PP government were the reduction of capital gains tax in 1996, a new tax regime for small-and-medium-enterprises (SMEs) and the Taxpayer's Statute²² in 1998 (Comin, 2006).

Having met the Maastricht criteria and secured their spot in the EMU, the PP turned its attention to reforming the personal income tax by way of reforming *Ley 40/1988*. The updated law incorporated new international trends which reduced the tax burden on low incomes and salaries, decreased the marginal tax rates so that savings would not be negatively affected, encouraged long-term savings and simplified the tax returns forms (Comín, 2007, p. 42).

The reduction of the tax burden in personal income tax led to a 4% increase in tax receipts in 1999 versus 1998 (Comín, 2007). The next reform to the personal income tax came in 2000 with *Ley 6/2000*, whose intent was to 'promote the internationalization of Spanish companies, to facilitate the adoption of new technologies, strengthening small and medium size enterprises, to protect the family unit and the most disfavoured social classes, and to encourage long-term savings' (Comín, 2007, p. 42).

As Comin (2007) points out, the results of the PP's tax reforms can be evaluated on the basis of collection figures. Income taxation collection decreased while receipts from indirect taxation increased, signalling an increase in consumption. Consumption increases can signal that the economy is growing and that there is confidence in the market.

The corporate income tax (CIT) was introduced in 1978 and has been in a constant process of adjustment, with a major reform in 1995. The continuous minor reforms signal that leaders were

²² Estatuto del Contribuyente, Ley 1/1998

trying to adapt the economy to changing conditions. The original CIT was set at 33% and increased to 35% in 1983 (Gomez, 2007), where it has remained since²³.

The result was a decreased burden on individuals but an increased burden on companies. The reform promoted growth in tax receipts by the state and contributed toward the decrease in the budgetary deficit.

3.1.4 Concluding remarks

Spain today finds itself in a precarious situation. The new government must implement strict reforms imposed by external actors in order to safeguard its future in the Eurozone. The government is facing national discord as citizens are protesting against changes and international tensions as financial markets are punishing the country for implementing reforms now that should have been addressed earlier. The latter situation refers to the driving up of interest rates demanded by the markets in order to buy Spanish bonds. This makes raising money and refinancing increasingly difficult for Spain, which in turn has repercussions on domestic issues. To avoid replicating the disastrous bond differentials and overall perilous situation of Greece, real reforms must now persevere in Spain.

²³ At the time of writing, corporate tax rate has been reduced to 30%

3.2 Greece

Overview

Following the Second World War, Greece was amongst the recipients of financial aid from the Marshall Plan in the 1950s and began to make strides economically. Having had joined NATO in 1951, and having received substantial monetary support from the Americans (in part as an offensive to fight communist sympathies in post-war Europe) the George Papandreou-led government suddenly found itself at odds with the Americans, mainly regarding issues with Cyprus. Tensions arose and were amplified until 1964 when President Johnson threatened to end aid to Greece if common ground could not be reached regarding Cyprus (Hastedt, 2004). Tensions subsided momentarily but arose again in 1967 which led to military action. Despite being lauded as the birth-place of democracy, a dictatorship emerged in Greece in 1967 with the establishment of a military junta until 1974.

Though Greece had achieved rapid economic growth thanks to large (mainly American) foreign investments in the 1960s, by the mid-1970s its GDP rate and the ratio of investment to GDP began to decline, leading to increasing labour costs. The authoritarian government did not address the structural problems at the onset, but the persistence of the economic crisis forced the military government to begin reforms, many of which paved the way to democracy. Indeed, movement towards democracy became the only way to achieve membership into the EC which was seen as the only viable way out of the economic crisis.

In order for Greece to join the European community in 1981, protective economic barriers had to be removed. To this end, the Greek government pursued aggressive economic policies, which resulted in high inflation and created debt payment problems.

3.2.1 Political Forces

1974-1981

The moderate-right government, New Democracy (ND) took control of re-establishing democracy in Greece and formed the first two majority governments of the post-authoritarian period, 1974-77 and 1977-81 (Ethier, *Economic Adjustment in New Democracies*, 1997). The ND spearheaded the negotiations with the EC and signed Greece's EC membership treaties (1976-79). The ND governments pursued expansionist economic policies which led to a strong increase in government spending leading to higher external debt and public deficits. They also invested in improving education, health and pension systems in order to consolidate democracy and bring Greece's social policies in line with those of EC member states (Davaki & Mossialos, 1994) (Sissouras & Amitsis, 1994).

The ND government undertook nationalization programs aimed at propping up economic sectors in difficulty. Unfortunately, the government's nationalization policy contributed to the deterioration of the Greek economy which was compounded by the recession following the second petroleum crisis of 1979 (Ethier, *Economic Adjustment in New Democracies*, 1997).

1980s

Greece became the tenth member of the European Community on 1 January 1981. The turn of the decade saw the election in 1981 of the socialist party, the Pan-Hellenic Socialist Movement (PASOK) led by Andreas Papandreou. This period continued to be marked by the economic crisis but the PASOK government did not deviate greatly from its predecessor regarding economic policies and maintained a Keynesian approach.

The PASOK government realized that it needed to renew production so it implemented demand-side measures financed by loans and foreign aid which led to an increase in the budget deficit (Ethier, *Economic Adjustment in New Democracies*, 1997). These measures consisted of increasing low and middle class earnings; broadening access to state retirement plans; augmenting social benefits both in scope and accessibility; indexing salaries retroactively to the cost of living; and a vast public works program aimed at creating jobs (Ethier, *Economic Adjustment in New Democracies*, 1997). From 1981-1985, the government continued the policy of bailing out the private sector by financing the deficits of 44 failing companies, nationalizing ESSO-Greece and creating a state pharmaceutical industry (Ofakoglou, 2012). It should be noted that the PASOK government was highly critical of business elites (Lavdas, 1997, p. 151) and sought to emphasize infrastructural support and financing of small businesses, a key aspect that contributed to the development in taxation schedules, as will be discussed in a later section.

The public sector, too, was in need of reform in order to function as the ‘motor of growth and modernization’ (Lavdas, 1997, p. 151) that the PASOK government wanted it to become. For this reform to take place the PASOK government pursued ‘economic adjustment and the promotion of development and growth’ (Centre for Economic Policy Research, 1985, p. 1). During its first mandate, PASOK published its *1983-87 Five Year Plan*. This plan, carried out between 1983 and 1985, aimed to redress the ‘external and internal imbalances in the Greek economy’ which existed due to long-term structural problems, external shocks and pre-1983 policies (Centre for Economic Policy Research, 1985, p. 1). Despite having outlined a variety of stabilization measures (SM²⁴s) to

²⁴ Specific policies aimed at bringing about stability in the economy. Can refer to demand management where business cycle stabilization is sought or exchange rate or inflation stabilization where economic crisis management

undertake, PASOK did not carry out any of the SMs outlined in the *1983-87 Plan*, with the exception of devaluating the drachma by 16% in 1983 and 15% in 1984 (Lavdas, 1997). Similarly, the *Plan* laid out structural change mechanisms (SCMs), though government action was even more limited on SCMs. In relation to SCMs, PASOK did ratify the framework law on higher education in 1982 and a law respecting ‘the socialization of political enterprises’ in 1983, which limited the exercise of the right to strike by introducing the rule of absolute majority to justify a strike (Ethier, *Economic Adjustment in New Democracies*, 1997, p. 46). This effect was offset by giving workers’ representatives continuous direct control over the management of companies.

Nevertheless, voters were not deterred by the lack of follow-through and thanks to the credibility garnered by its economic program and, as has been suggested by Tsarouhas (2012), the lack of a viable alternative, PASOK secured a consecutive second term in the elections of June 1985. PASOK’s first term in office can be categorized as gradual adjustment to its new European reality as PASOK’s term coincided with the entry into effect of Greece’s EC membership treaty.

The first PASOK government had been elected on an anti-EC agenda, demanding a ‘special relationship’ with the EC (like Norway or Yugoslavia) (Pagoulatos, 2002, p. 2) and not really understanding the responsibilities or capacities of the EC system, as evidenced by the large number of Greek violations of, in particular, EC competition law and delays in implementing EC legislation on a wide range of issues, in general (Pagoulatos, 2002). Once re-elected, and contrary to the campaign promises made, PASOK began to pursue a more liberal economic policy, motivated in large part by the desire to obtain a new loan from the EC (Pepelasis, 1990).

is required. Generally carried out via fiscal and monetary policies.

The second Papandreu PASOK government adopted a stabilization program that targeted reducing inflation, reducing the balance of trade deficit and reducing the budget deficit.

The program resulted in higher interest rates; a 15% devaluation of the drachma; a less generous salary indexation policy; fixing the price of agriculture products below the inflation rate; 4% decrease in financing needs over public companies due to stricter control over public spending and tax fraud; creation of special tax on corporate profits, incomes of self-employed and rents; closure of some public companies and other important but less relevant changes (Ethier, *Economic Adjustment in New Democracies*, 1997). Structural reforms were also pursued, this time in earnest, with the intent of bringing Greece in line with the requirements of the membership treaties and the Single European Act (SEA). A shift is observed towards a milder anti-EC stance, both in rhetoric and actions.

In 1987, PASOK introduced the value-added-tax (VAT) system, liberalized legislation on foreign direct investment (FDI) and regulation of the financial sector and adopted legislation aimed at establishing gender equality in the workforce.

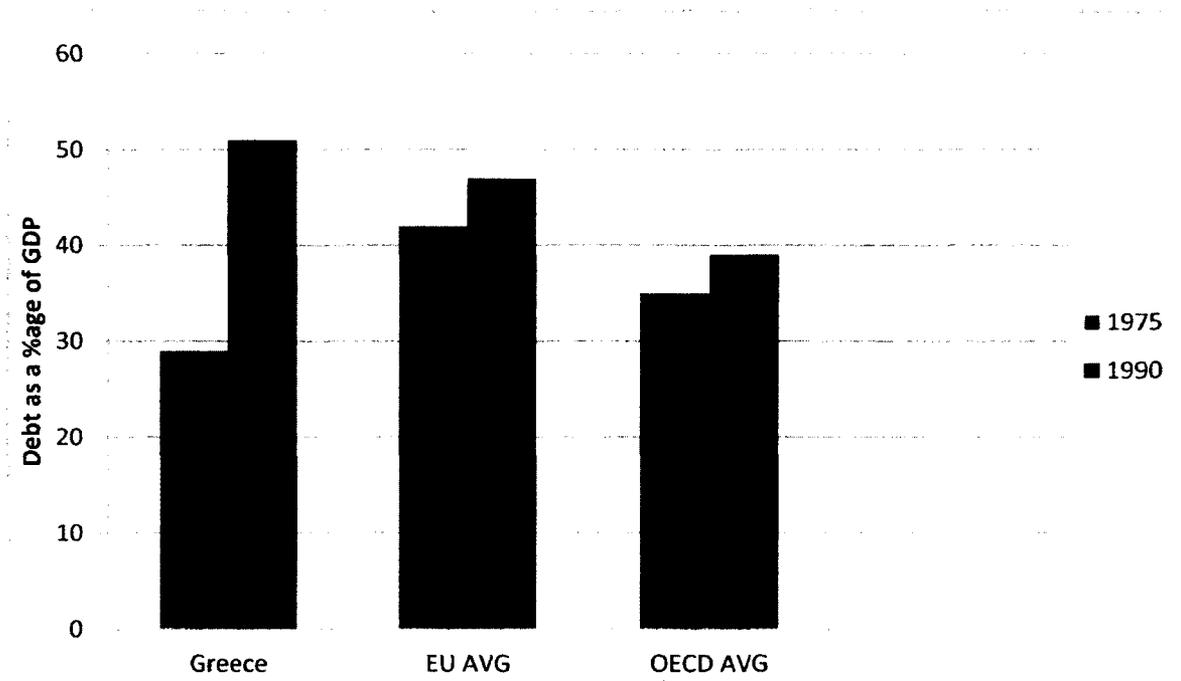
Positive effects were observed for the period 1985-1989. Inflation decreased from 25% to 14%; unit cost of labour was halved, financing needs of companies decreased from 18% to 13%, unemployment was reduced from 9.7% to 8%. While positive, these reductions were not sufficient to renew investment and production and the government debt and budgetary deficit continued to grow while companies still had productivity and competitiveness problems due to insufficient decrease in labour costs. As it can be seen in

Figure 8, following the end of the military junta, Greece was spending far below (about 29% of GDP) the European average (42% of GDP) and the average for the OECD countries (35% of

GDP). Over the next 15 years, the governments pursued a course of spending, incurring debt, which brought the Greek ratio, 51% of GDP, well above both the European average in 1990, set at 47% of GDP, and the OECD average, which had increased to 39% of GDP. While increased indebtedness was a general trend, as shown in

Figure 8, the Greek debt incurred during this period massively outpaced the average of its counterparts, reflecting the will of the politicians to converge with little regard to the structural problems such a rapid increase might impose.

Figure 8: Greek Government Spending, %GDP



Source: OECD 2001

From June 1989 to April 1990 the economic situation continued to deteriorate and the inability of political authorities to deal with the problems increased. Amidst a growing number of corruption scandals, the mismanagement of monetary and fiscal policies and declining international competitiveness, Papandreou’s PASOK could not stay afloat and elections were called.

1990s

New Democracy (ND), the right-wing party, led by Konstantinos Mitsotakis, formed a majority government in April 1990 (Lavdas, 1997). The ND sought a major adjustment program that aimed to decrease the inflation rate by 10%, decrease the civil servant labour force by 10%, slash public sector funding in half, privatize many public companies, reform the social security, labour laws and national social laws through the adoption of certain limited-range legislative measures (Skouras, 2001).

The implementation of this program was met with many obstacles and resulted in only partial improvements in economic imbalances. By 1991 inflation had dropped 5 points and the balance of trade deficit had stabilized but the public deficit to GDP ratio increased from 8.7% to 9.2% and GDP growth remained negative (-1.0) while investment stagnated. The stabilization plan led to strikes by trade unions that demanded that privatizations would not encroach on employment security. As a result, the privatization process was not effectively started until March 1992 due to the difficulties in attracting investors and resistance from labour unions (Ethier, Economic Adjustment in New Democracies, 1997).

1992 saw a great achievement towards Greece's European goal, with the Greek parliament's ratification of the Maastricht Treaty (TEU). Mitsotakis used the occasion to state his government's 'resolve to have Greece accepted' into the economic and monetary union (EMU), though observers pointed out that Greece would be unable to meet the convergence criteria set for the implementation of the 1st phase of the EMU unless it restructured its economy dramatically and changed mentalities (Ethier, Economic Adjustment in New Democracies, 1997, p. 49).

Since the Mitsotakis government has been reduced to a minority position it was not able to carry out the necessary reforms needed to qualify at that time. Early elections were called in September 1993 (Ethier, *Economic Adjustment in New Democracies*, 1997).

PASOK returned to power from 1993-1996 and kept with the SCMs undertaken by the ND and pursued supply-side expansionary policies. Promises were made, including a reform of the tax system, but the illness, and subsequent death, of Papandreu left Kostas Simitis, the leader of the liberal faction, in charge (Ethier, *Economic Adjustment in New Democracies*, 1997). Simitis found himself in power but unable to make any radical changes due to the lingering legacy of Papandreu within his own government and their socialistic tendencies to refuse liberal changes in economic policies. PASOK won the 1996 and 2000 elections, though narrowly, as Simitis consolidated his power and support by promising to bring Greece into the euro.

2000s onward

On January 1, 2001, Greece joined the Eurozone. PASOK's support for liberalization, deregulation and entry to the euro-zone created a stock market boom which made the party popular with private industry. Greece's adoption of the euro was accompanied by a rapid increase in salaries and pensions and employment in the public sector. Public-sector wages rose considerably under the Simitis government. When ND came back to power in 2004, the new Karmanalis-led government maintained the salary increases of the public sector but ordered a fiscal audit of the preceding government's efforts to join the Eurozone. Revisions of the original data revealed that the PASOK government had claimed that Greece's deficit was less than 1% of GDP though European Commission reports revealed that Greece's budget has not been within the 3% limit since its accession (Wienberg, 2011). PASOK countered that they had not lied, but that the different numbers came from the different types of accounting methods accepted by Eurostat (Pappas,

2010). Eurostat did partially agree and changed its accounting methods, but also underlined that it believed that the Greek government had been systematically under-reporting and had made no attempts to address the systematic problem (Wienberg, 2011). Debate continues between PASOK and ND on the accuracy of the figures, but politics aside it is now generally accepted that statistics related to the Greek budget and inflation figures have been subject to systematic distortion. Given the current chaos characterizing Greek politics, years may yet pass before we know the true extent of distorted data.

One additional, related, aspect worth analyzing for Greece is corruption and the effects it has on the economic activity of the country. Corruption is a well-known mainstay of the Greek political system and economy. By 2009, of the EU member states, Greece was seen as among the most corrupt, rivaled only by Bulgaria and Romania (Pop, 2009). Quoted from its 2009 report, Transparency International concludes that 'Greece's poor score shows that joining the EU does not automatically translate into a reduction in corruption. Immediate and sustained efforts are required to ensure the country lives up to acceptable levels of transparency and accountability' (Pop, 2009, p. 1).

'Graft and corruption have always been an integral part of Greece's political culture, thanks to the existence of a paternalistic state where kickbacks constitute routine practice for the provision of public services' (Pop, 2009, p. 1).

The basic structure of the criminal laws against corruption, as described by Konstantopoulou (2003, p.260) are described as 'not a unified whole.' The Greek Criminal Law on Corruption is constituted by a variety of provisions found both in the Special and the General Part of the Greek Penal Code (GPC), as well as in Special Criminal Laws, of which some criminalize special forms

of corruption, while others integrate international legal instruments on corruption into the Greek legal system (Konstantopoulou, 2003). The lack of clear and consistent rules and consequences create a gray-area of permissibility where some acts of corruption are indictable by the penal code, others are treated as misdemeanors yet still others go unpunished.

One Greek law -N. 2509/1997- made it very difficult to prosecute ministers and members of parliament for crimes committed while in office. The law was introduced by the PASOK government in 1997 after a prior conservative government had prosecuted for corruption four PASOK ministers and a PASOK prime minister (Andreas Papandreou²⁵) retroactively. Basically, the law reduced the statute of limitations for parliamentarians and ministers for being indicted of corruption charges. Specifically, Article 86 of the Greek Constitution²⁶ states that ‘a cabinet Minister can only be prosecuted after the consent of the Parliament sitting in plenum has been obtained. Such consent must be obtained before and no later than completion of the second regular session of the parliamentary term, which started after the offence was committed, otherwise the crime cannot be prosecuted’ (Transparency International Greece, 2010). This law has far-reaching implications that must have been obvious to the government. Such a provision can serve as insurance to politicians that they can and will get away with anything provided they time it correctly and do nothing to curb or even discourage corrupt practices.

²⁵ An obituary of Andreas Papandreou written in *The Economist* (1996) states that ‘Perhaps his most remarkable achievement was that, after he won power in 1981, a solid two-fifths (or more) of the Greek people continued to vote for him... however corrupt his inner court of cronies..’.

²⁶ Full text available at <http://www.hri.org/docs/syntagma/>

In 2004 Konstantinos Karmanalis promised to reform the country, but the only thing he delivered was scandal. His administration falsified financial data sent to the EU, shifted money out of retirement funds, created tens of thousands of administrative posts for friends and relatives, and doubled the national deficit (Lopez, 2011).

2005 saw a concerted effort by the General Inspector for Public Administration to clamp down on corruption. A special report published in July by the Greek general inspector of public administration concluded that the public sector is riddled with corruption. Urban planning offices, state hospitals and town halls were identified as the sectors where corruption is most acute.

In 2006, Transparency International reported that Greece was introducing a new law in order to increase the monitoring and transparency within the judiciary, including a more serious categorization for the crime of attempting to bribe a judge and a new code of conduct for public officers. This law was a welcome attempt to address the prevalence of corruption not only in the higher and executive branches but at all government levels.

Despite an apparent will for change, the Corruption Perception Index (CPI) shows a different picture. The CPI defines corruption as "the misuse of public power for private benefit "and ranks 178 countries on a scale from 10 (very clean) to 0 (highly corrupt). In 2005, Greece scored 4.3 out of 10 (Manolopoulos, 2011). By 2009, Greece's corruption perception had increased to 3.8 out of 10, a clear indication that despite rhetoric, corruption was on the rise.

Table 1 shows all respective rankings from 2002 to 2011. An improvement is recorded from 2002 until 2008 when a stark deterioration can be seen, on the cusp of the crisis, which reignited the debate on the credibility of financial and monetary reporting in Greece.

Table 1: Corruption Perception Index Greece, 2002-2011

	2011	2010	2009	2008	2007	2006	2005	2004	2003	2002
80  Greece	3.4	3.5	3.8	4.7	4.6	4.4	4.3	4.3	4.3	4.2

Source: Corruption Perception Index, 2012

Additionally, a Brookings Institute study in 2010 found that bribery, patronage and other forms of public corruption are major contributors to Greece's public debt. While focus tends to centre on corruption within the public sector, corporate corruption scandals are not uncommon in Greece. A few notable cases include Siemens, Ferrostaal and Daimler (Manolopoulos, 2011).

3.2.2 Structural Labour Reforms

Starting in the 1980s, the public sector has expanded as all ruling parties used their positions to reward supporters with jobs. Currently, '20% of the working population is some sort of civil servant, in a job that has been guaranteed for life under the constitution' (euronews, 2011). The public sector is notorious for its inefficiencies, but thanks to the generous compensation provided, attempts at decreasing its size have always been met with protests.

The Greek labour market is weak in terms of flexibility, despite policies pursued to address unemployment.

The competitiveness of the Greek economy is often ranked below that of its fellow Eurozone member states and most members of the OECD. The *World Bank Doing Business* reports rank Greece 109 out of 183 economies in 2010 for the ease of conducting business. While not a perfect or complete analysis of the variables, the ranking looks at a number of important indicators for conducting business. Among the relevant ones when analyzing labour market functionality in

Greece are ‘Starting a Business’, ‘Employing Workers’ and ‘Enforcing Contracts’, as presented below.

Table 2: Ease of Doing Business in Greece, 2010

Indicator	Ranking in Doing Business 2010
Starting a Business	140
Employing Workers	147
Enforcing Contracts	89

Source World Bank 2010

These indicators are certainly not exhaustive in providing a snapshot of the Greek market. These indicators do, however, address some of the most important milestones in the chronology of starting a business. Being ranked 140th out of 180 countries for starting a business reflects the rigidities of the administration in terms of the number of procedures required to effectuate the establishment of business, the time delay, the cost and the capital requirements. Indeed, Greece requires 15 separate procedures before a business is established, situating it alongside countries like Bolivia and the Philippines, who require the same number. To provide contrast, in Canada, New Zealand and Australia, the leaders in ease of procedures, only one procedure is required to start a business (World Bank, 2010).

Secondly, and very pertinent as regards the labour market, employing workers is a long and difficult process, as Greece’s rank of 147th shows. This means that it would be simpler to employ workers in 146 other countries, including Spain, Slovenia and Slovakia. Enforcing contracts is

another indicator that is concerning as regards the trust between investors and employees. Those wishing to start a business and employ workers are deterred from doing so because they question their ability to enforce the terms of agreed-upon conditions in the contracts.

As seen above, the ability to employ workers is limited in Greece, an especially acute problem for the youth. The low unemployment amongst youth indicates the persistence of serious qualitative failures in the labour market in spite of the gradual decline in unemployment (Mitsopoulos & Pelagidis, 2011).

The labour market's failure to create new jobs is directly linked to the lack of dynamism established by supply-side economics further aggravated by the excessive regulations and administrative burden.

The employment rate among youth is particularly troubling and should be brought to the forefront of monitoring. As pointed out by Mitsopoulos & Pelagidis (2011), any determined effort to deal with the deep and widespread structural problems of the economy will be most prominently reflected in the employment rate of the youth.

Greece is among the OECD countries with the most restrictive employment protection legislation (EPL) foreshadowing rigidities especially in the non-permanent and temporary employment sector, with a very limited use of temporary contracts (Mitsopoulos & Pelagidis, 2011).

In addition, we observe in Greece a very large number of private sector employees who declare themselves 'self-employed' and work exceptionally long hours. It would appear that the economy goes to great lengths to avoid the use of 'salaried labour' (Mitsopoulos & Pelagidis, 2011, p. 141).

On the other hand, a large public sector exists. Remuneration in the public sector is the central feature of its attractiveness. Compared with the Greek average monthly wage of about €700, a civil servant starts at €800, and bonuses can increase that amount to €1,300 a month (euronews, 2011). Additionally, employment in the public sector is secure and public servants once hired enjoy lifetime contracts and cannot be discharged, except for misconduct. In Greece, public sector wage increases were given by cost of living and budget conditions, and private sector comparability is not a standard (European Central Bank, 2011).

Given the large proportion of Greek workers that are employed by the public sector and their generous remuneration, it is no wonder that pressure has been consistent and strong to maintain the system's status quo.

Labour Unions

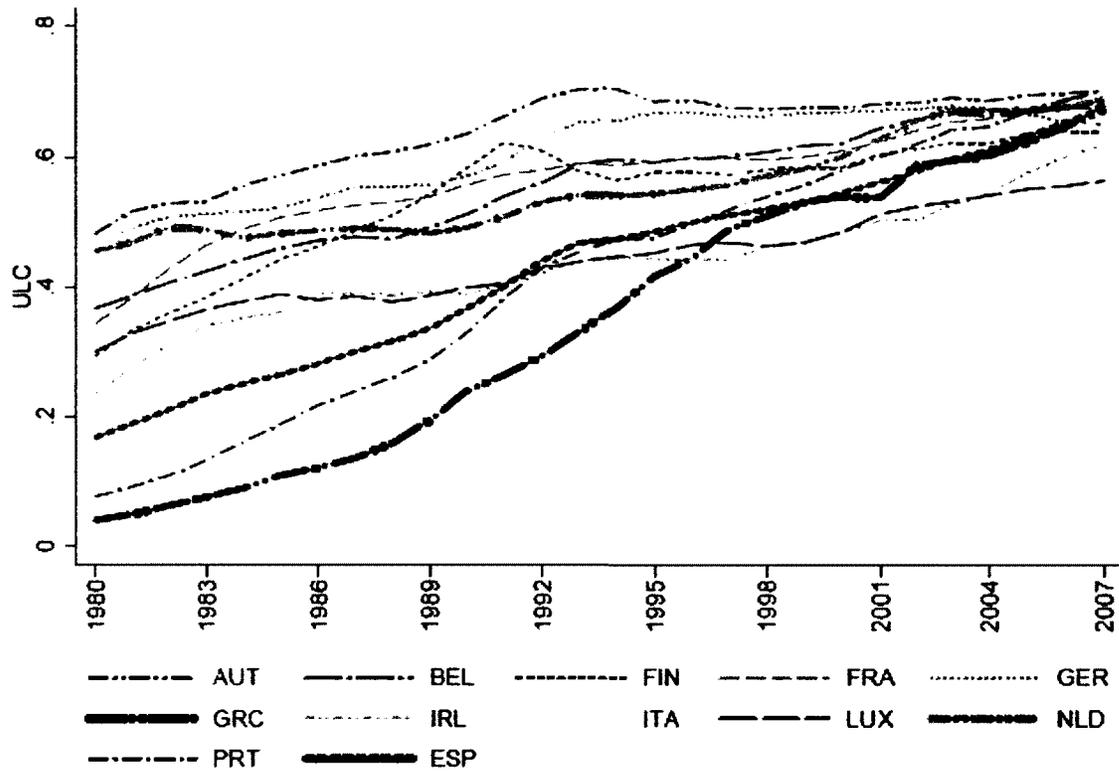
In the 1980s and 1990s little difference arose regarding the approach to labour unions. Neither the PASOK nor the ND governments wanted or dared to confront the public sector trade unions (Manolopoulos, 2011, p. 85). In Greece, public sector pay is determined by law, according to the government's annual income policies. This law was passed in 1999 and recognizes the right to collective bargaining in the public sector. Pay issues are, however, excluded from the bargaining procedure (European Central Bank, 2011).

Consequently, it is still very difficult to fire employees in the public sector. Not only can employers not downsize their workforce when demand and other internal pressures demand it, but trade unions have ensured, according to an International Monetary Fund (IMF) report in 2012, that 'Greece's entry-level minimum wage is higher than in Portugal (by 50%), Spain (by 1%), and 5–7 times higher than in Romania and Bulgaria' (IMF, 2012, p. 6). The IMF argued that an internal

devaluation is necessary to improve Greek competitiveness. The program stipulated by the IMF aims to make collective bargaining more effective, reduce the minimum wage, and lower nonwage labour costs. The report maintains that measures to liberalize services would also help to improve the competitiveness of the Greek economy. If riots in Greece for the past two years are any indication, neither labour unions nor employees themselves understand the prescription or are willing to try the IMF's medicine. In a country where labour unions are so strong and have the ability to paralyze an already-weak economy, reform of the labour market, though necessary, is not easy.

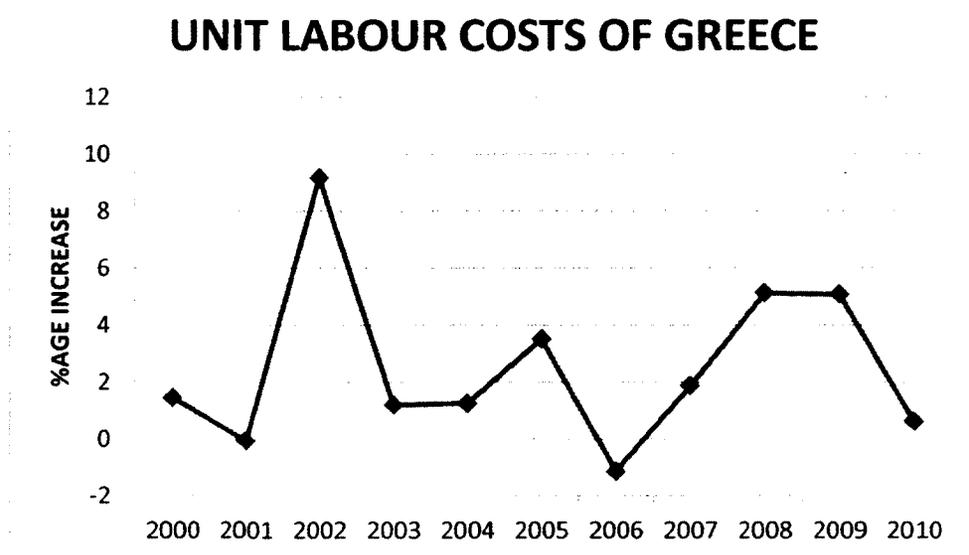
To explain the lack of competitiveness we look at ULCs, which have a direct impact on productivity. Figure 9 below demonstrates that while unit labour costs were initially lower in Greece, they have been on a steady increase since the 1980s. In fact, Figure 9 shows clearly those countries that are regarded as leaders in competitiveness, namely Luxembourg and Germany, have had unit labour costs since 1995 lower than those in Greece. This suggests that ULCs and wages need to be revised in Greece as costs are outpacing productivity, which can add to competitive problems. Figure 10 further shows that Greece only responded to the need to decrease ULCs once the crisis was well underway, reinforcing Greece's use of reactionary rather than proactive reforms.

Figure 9: Unit Labour Costs in the Eurozone, 1980-2007



Source: Felipe & Kumar (2011)

Figure 10: Unit Labour Costs Greece, 2000-2010



Source: OECD data, 2012

Pensions

Between 2001 and 2007, employment amongst those aged 15-65 improved, but a significant proportion of that population now is over the age of 65, making gains in employment only short-lived, and exacerbating other problems related to an aging society (Mitsopoulos & Pelagidis, 2011).

Reforms of the state pension system were aimed at reducing the disparity and income inadequacy for the elderly. While a robust pension system can help fight old-age poverty, it has serious fiscal implications that a small, uncompetitive state like Greece cannot shoulder.

Table 3 summarizes the divergence between retirement expectations in Greece vis-à-vis the OECD average. Not only can Greek workers retire before their OECD counterparts, but their pensions are also far more generous. This raised a red flag about the sustainability of the pension system in Greece and led to EU-sanctioned reforms.

Table 3: Retirement Age and Level of Pension Prior to 2010 Reform

	Official Age of Retirement	Average Pension, % of average lifetime earnings
Greece	58	95.7
OECD	63.2	60.8

Source Manolopoulos (2011)

Until the 2010 pension reform (accompanied by both peaceful and violent protests), the average Greek pensioner was able to retire five years earlier than his OECD counterpart with a pension that was 35% greater.

There is a large burden imposed on the Greek economy by, on the one hand, the aging population referred to earlier, and on the other, ‘the practice of allowing employees (mainly in state-controlled companies and public sector branches)’ to retire early and with generous provisions (Mitsopoulos & Pelagidis, 2011, p. 139).

In the early 1990s, the ND attempted two pension reforms (laws 1902/90 and 2084/92) by reducing replacement rates, increasing contribution rates, and increasing the retirement age to 65 years (Tsarouhas, 2012). The indexation of pensions to wages was discontinued, while seniority pensions were cut for those entering the labour market after 1993 (OECD, 2005). However, ‘the structural deficiencies of the Greek pension system were left untouched’ (Tsarouhas, 2012, p. 165).

Following PASOK's re-election in 2000, the government commissioned a study by Government Actuaries and in 2001 published its proposals for reform, the 'Giannitsis proposals' named after the Labour minister at the time (Tsarouhas, 2012, p. 166).

The main reforms entailed setting the replacement rate to 80 per cent of previous earnings, the gradual increase in retirement age to 65 for men and women, the rise in insurance period permitting seniority pensions from 35 to 40 years, the introduction of disincentives for early retirement and the rise of the minimum pension that would become means-tested (Triantafyllou, 2008).

Though the reform did not suggest an overhaul of pension structures it addressed some of the gross inequities of the system (Matsaganis, 2008). The proposals were immediately attacked by the union leading to countrywide strikes (Tsarouhas, 2012). Giannitsis was removed from office and the original proposals were buried (Tsarouhas, 2012). Law 3029/02, passed once Giannitsis was out of office, was a significantly 'softer' version of the original proposals (Tsarouhas, 2012, p. 166). No projections as to the pension deficit were made and no change in the retirement age was proposed (Tsarouhas, 2012).

In the years following, minor changes were made to the pension system. Pensions increased in 2004 by 3%; in 2005 by 4% and in 2006 by 4% (Manolopoulos, 2011, p. 88). To contextualize these expenditure increases, during the same time period, the increases in Germany were 0%, 0% and 0%, respectively.

After the 2002 legislation no major changes occurred until 2008, when the government opted for mostly administrative changes, primarily the amalgamation of insurance funds. (Tsarouhas, 2012)

Recent (2010) pension reforms, well outside the scope of this work, have been more radical and accompanied by a new pension law²⁷.

Surprisingly, an OECD (2007) report found that the Greek contribution-based unemployment benefit is among the least generous in the OECD. In fact, the Greek benefit equivalent was only 4% of the average wage (OECD, 2007). That being said, unemployed persons are able to register and receive benefits even if they are not actively seeking work as monitoring is weak.

3.2.3 Taxation

Analysis of the Greek taxation system must be framed in the perspective of a system categorized by low ‘tax morale’, loopholes and corruption which have reinforced an environment for widespread tax evasion. Of about 11²⁸ million Greek citizens, only 5000 admit to annual earnings exceeding €100,000, despite records that show that more than 60,000 Greek households have investments exceeding one million euro (Hope, 2010). One Athens-based developer told the *Financial Times* that Greek companies believe that corruption is widespread among tax officials and so ‘[i]t’s much easier to agree on an under-the-table payment than challenge your tax assessment through the legal system’ (Hope, 2010). A Greek term, *fakelaki*, meaning ‘little envelope’ is now used to describe the bribing of public servants (with small envelopes stuffed with money) by Greek citizens looking to expedite services, secure appointments and gain approval for

²⁷ Most important changes of Law 3863/2010: reduced notice period for terminating employment agreements, lower thresholds for collective dismissals, reduced overtime costs, decreased the minimum wage for workers under 25 years of age to 84% of the minimum national wage

²⁸ The CIA World Factbook estimates the figure to be 10,767,827 as of July 2012.

permits.

Citizens, despite taking advantage of the system, admit its flaws. In a recent 2011 survey conducted by the Institute for Financial and Tax Analysis, nine out of ten taxpayers declared that the tax system in Greece is not stable, and eight out of ten characterized it as unreliable and socially unjust. 74% of respondents answered that the tax system is inefficient, 71.4% said that it is non-transparent, and 84.4% that it does not favour competitiveness (GRReporter, 2011). Citizens' distrust and lack of confidence in the tax system and its administration are factors contributing to tax evasion, but corruption and permissibility impede the system from achieving real reform.

Income tax^{29 30} in Greece is progressive with the highest tax rate of 45% applicable to income over €40,000. Though tax rate brackets give the impression that they would provide substantial government revenue due to tax evasion and under-reporting of income, the highest tax rates are seldom applied. Income under €7,000 is not taxed.

Tax evasion at the corporate level is carried out mainly by smaller and low-technology companies (Manolopoulos, 2011). Attempting to correct this shortfall, governments have increased the taxation on larger and high-technology companies, hampering their profitability and deterring companies from choosing to pursue business in Greece (Manolopoulos, 2011).

²⁹ Taxable income is any income that derives from any of these sources: Real estate income, income from non-fixed values (stocks, loan interest etc.), trade, agriculture, employment and independent labour.

³⁰ Law on Income Tax: 2238/1994, as amended by Law No 2579/1998 (Government Gazette I,31A/17.2.1998) Law No 2992/2002, and Law No 3091/2002

In 2007 the rate of corporate tax was set at 25%. Originally, the government had designated that as of 2010, the corporate tax rate would fall 1% annually reaching 20% in 2015. However, ahead of schedule, in 2011 PASOK introduced a uniform rate of 20% and introduced a 25% withholding tax on dividends (Reuters, 2011).

Greece is unusual among EU countries in the large share of indirect taxes³¹ in total tax revenue (60% compared to an average of around 40% for the OECD countries or the EU-15, (OECD, 1999)), and the considerable variation in individual indirect tax rates. This variability in tax rates results from the large number of different taxes levied often on the same good which survived even after joining the European Union and adopting the EU system of VAT.

The heavy emphasis on indirect taxes and their variability have survived substantial tax reforms that have raised Greece's tax share in GDP from 24% to 37.4% from 1980 to 1999, though the share of indirect taxes in total revenue has fallen from 70% to 60% over that period (Ministry of Finance and Economy, 2001). The introduction of VAT in the late 1980s simplified indirect taxes somewhat, and since then there have been further but modest simplifications. (Kaplanoglou & Newbery, 2002).

Presently, the VAT tax in Greece ranges from 6.5% to 23% (BBC, 2011). For all goods not belonging to any special category, the VAT is 23% (The new VAT rates from July 1, 2010). The reduced rate - applicable to goods such as fresh food products, pharmaceuticals, transportation and

³¹ Law on the VAT: 2859/2000

electricity, as well as to certain professional services such as those supplied by hotels, restaurants, coffee shops and (non-exempt) services by doctors and dentists – was increased to 13 % as of January 2011 (up from 9 % in 2009) (Eurostat, 2011).

3.2.4 Concluding Remarks

As summarized by Bryant et al (2001), the 1980s was a period of fiscal expansion which led to a marked increase in public debt (see section 3.2.1 Political Forces) which has been linked to further increases in the structural weaknesses of the economy, a deterioration of the regulatory environment, poor growth numbers and increased unemployment and inflation. The 1990s witnessed Greece's resurrection relative to its growth performance vis-à-vis the other European member states, but real and necessary reforms to address structural weaknesses in its labour market and taxation (both structure and collection) were not carried out, mostly because of weak political will and a political culture dominated by corruption. Procrastination has caught up with Greece and it now finds itself in a situation where external stakeholders are dictating the terms and conditions of reforms. Real reform cannot be falsified and convergence with European standards can only come about once structural economic problems have been addressed.

3.3 Slovenia

Overview

As the westernmost of the six republics that formerly combined to make Yugoslavia, Slovenia is a special country, in demographics and transition path.

Yugoslavia was a political community that was explicitly established as a trans-national union of states/republics (Debeljak, 2011). In the 1950s, Yugoslavia broke with the dysfunctional Soviet-style social and economic system following a period of economic stagnation, growing tensions with the Soviet Union and a Soviet-bloc trade embargo (Debeljak, 2011). The elite realigned their ideology to the writings of Marx and pursued a new economic system called socialist self-management. Laws were passed in 1950 and 1951 to implement this new system which replaced state ownership of the means of production with social ownership, entrusting management to the workers of each enterprise (Jonsson, 2006). The law empowered the workers' councils in terms of setting production goals and supervising finances but government-appointed directors retained veto power while foreign trade remained under central control (Debeljak, 2011).

Decentralization required the freeing of prices and the loosening of decision-making by the Communist Party. The change was not so dramatic as to allow for multiparty pluralism to develop in the political system, but intraparty debate was given room to decide party policies. Importantly, travel restrictions were eased, allowing the Yugoslav population more contact with western ideas and ideology. Political dissidents were not well-tolerated, but there was more room for disagreement than in the Soviet-bloc.

Development was not constant across all the republics, reducing the ability of more-advanced Slovenia to modernize due to the need to tackle growing regional imbalances and disparity (Debeljak, 2011). This produced resentment towards the other republics, which increased as Serbia and Montenegro sought to obstruct reforms throughout the 1960s (Debeljak, 2011). Intellectual and technical elites rose to the forefront in the 1980s as pronounced national differences divided the Communist Party.

In 1989 the Front for Independent Slovenia appeared with demands for total independence. Slovenia was the first Yugoslav republic to hold multiparty elections, in early 1990. The dissolution of Yugoslavia paved the way for Slovenian independence in 1991.

Slovenia was 'one of the smallest of the Yugoslav republics and the most developed, strongly oriented to exportation, especially to the EU' (Lavrac & Majcen, Economic Issues of Slovenia's Accession to the EU, 2006, p. 1). That the border was open due to its proximity to Austria and Italy helped the Slovenes to put into perspective the importance of the EU and its market.

The transition in Slovenia occurred at different levels. There was the initial transformation from a socialist to a market economy. Secondly, there was the need to redirect the regionalized economy towards a national economy. And third, though simultaneously, was the realignment from being part of Yugoslavia to joining the EU.

Slovenia approached transition with a calm gradualism, cautiously implementing the structural reforms required for EU accession. Unlike its neighbour to the northeast, Slovakia, Slovenia was against pursuing a 'big bang' approach, even when foreign advisers, headed by the IMF, suggested the alternative. Slovenia recognized that while a shock therapy would cut ties with the past paving the way for a new direction, it could also cause serious disruptions in the economy, leading to

temporary loss of output, a rise in unemployment and threaten political stability, which could have negative repercussions on the original economic reforms. Certainly, gradualism is not itself without drawbacks, such as the danger that structural reforms get pushed back and postponed slowing the entire transition process.

Gradualism made sense in Slovenia for several reasons. To begin, and as previously highlighted, Slovenia's advanced economic development in the region set it apart from its neighbours and the policy they pursued. Simply put, Slovenia could afford to take its time. Also, the initial position of its economy and its characteristics which had inherited some 'market economy characteristics from the Yugoslav system' contributed to the decision to pursue a conservative approach (Lavrac & Majcen, *Economic Issues of Slovenia's Accession to the EU*, 2006, p. 1).

The drawbacks to a gradualist adoption rate did begin to manifest. As the process of privatization was delayed, certain sectors were shielded from foreign competition (banking being amongst the most notable) and certain sectors saw glacial restructuring. The gradualist approach came under attack by various critics that felt it was time to see a more proactive and ambitious approach pursued (Lavrac & Majcen, *Economic Issues of Slovenia's Accession to the EU*, 2006). Structural reforms, higher economic growth and real economic convergence with the EU were necessary in order to deal with the competitive pressures in the EU market.

3.3.1 Political Forces

1990s

In May 1988, the Slovene Farmers' Alliance (SKZ) was established in Ljubljana, based on the Slovene Association of Cooperatives, and proclaiming itself a professional organization (Repe, 2010). In January 1989, the Slovene Democratic Alliance (SDZ), primarily a party of people

working in culture and the arts, was established. In February 1989, the Social Democrat Alliance of Slovenia was established, emerging from an independent union movement (Repe, 2010). Also in 1989, the Christian social movement strengthened; however, some of its members established their own party, the Slovene Christian Democrats (Repe, 2010). The Greens of Slovenia, too, were founded in that year (Repe, 2010).

The former socio-political organizations were also transformed into parties. The League of Communists of Slovenia (ZKS) became the Party of Democratic Renewal (later the Social Democratic Party); the League of Socialist Youth of Slovenia became the Liberal Party, and the Socialist Alliance of the Working People became the Socialist Party (Repe, 2010).

Amendments to the constitution in 1989 and 1990 restored to Slovenia the 'rights to manage national income and command their armed forces' (Jonsson, 2006, p. 74). Shortly thereafter, the League of Communists of Slovenia introduced a private and free market economy and left the League of Communists of Yugoslavia in January 1990, 'paving the way for Slovenia's first democratic elections since World War II' (Jonsson, 2006, p. 74). A new constitution was accepted on December 23, 1991, six months after declaring independence. A law was passed in the National Assembly which implemented the new constitution and stipulated that the transition (establishing the new political structures and positions) was to be completed in one year (Jonsson, 2006). Allowances were made for the applicability of federal laws where no republic laws existed and where the federal law did not contradict the new Slovenian constitution (Jonsson, 2006).

According to Repe (2010) the Democratic Opposition of Slovenia (Demos) coalition won the 1990 general elections with about 55% of the votes. Milan Kučan won the presidential seat in the second round of elections.

Slovenia introduced its own currency, the *tolar*, in October 1991 (Government Communication Office, 2010).

In April 1992, as a result of disagreements in the Demos coalition, Lojze Peterle's Demos government collapsed, and a new government, based on a broad coalition of the Liberal Democrat Party (LDS), the Socialist Party, reformed communists and half of the Demos parties, was formed by the LDS president Janez Drnovšek (Prunk, 2005). The LDS exercised a 'leading role' and implemented its 'liberal social and political model of development for Slovenia' (Prunk, 2005, p. 1). Kučan was the president of the republic and Drnovšek the prime minister.

Drnovšek formed his second government in December 1993 (Prunk, 2005); Slovenia signed an agreement of cooperation with the European Community and also joined the IMF and World Bank that year (Government Communication Office, 2010).

Formally, Slovenia expressed its intent for inclusion in the EU with the first 'Strategy of Economic Development in Slovenia' in 1994. Prime Minister Drnovšek and representatives of unions and employers signed the first social agreement in Ljubljana in 1995, and Drnovšek signed the *Spanish Compromise*, granting priority purchase rights to former Italian owners of real estate in Slovenia (this move served to put an end to Italy's blocking of Slovenia's accession process) (Repe, 2010, p. 1).

Slovenia's *Strategy of Foreign Economic Relations* of 1996 elaborated arguments for the inclusion of Slovenia in the EU and compared this path with alternatives like 'autarchy, direct globalization and inclusion in other regional organizations' (Jonsson, 2006, p. 75). Slovenia signed an association agreement with the EU and submitted its application for EU membership in June 1996 (Repe, 2010). In November, the LDS won the parliamentary elections and in February 1997,

Drnovšek formed his third government (Government Communication Office, 2010). Presidential elections in November 1997 saw the re-election of Kučan (Repe, 2010).

In its *Strategy for Inclusion in the EU* in 1998, Slovenia defined a number of structural reforms for accelerating the transition process and preparing its economy for EU accession. Negotiations with the EU began. Slovenia became an associate member of the EU the following year as its Association Agreement came into effect.

EU accession was well accepted across major political parties, becoming a sort of unifying project. That the nationalist party was opposed to the push to associate Slovenia with the EU came as less of a surprise than did the initial low support for integration with the EU. Some have argued that this was due to the mismanagement of public perception of new pressures from neighbouring member states during the EU accession negotiations. Public misgivings were resolved by the time negotiations wrapped up in 2003 as showcased by the ‘86% of Slovenes that voted yes’ to EU accession (Jonsson, 2006, p. 75).

2000 onwards

The Slovene Parliament passed a vote of no confidence to the third government of Mr. Drnovšek and the new prime minister became the president of the formerly opposition New Slovenia party, Andrej Bajuk (Government Communication Office, 2010). The new government was in office only until parliamentary elections in mid-October in which liberal democrats won and Janez Drnovšek formed his fourth coalition government with social democrats (ZLSD), People’s Party (SLS) and the pensioners’ party (DeSUS), which was elected into office at the end of November (Government Communication Office, 2010).

The European Commission (2000) recognized Slovenia's efforts in its *2000 Progress Report*, emphasizing progress made in the area of pension reform and citing the existence of a functioning market economy which would provide Slovenia with the capacity to cope with competitive pressure and market forces within the EU, following additional efforts to accelerate reforms aimed at improving competitiveness. In keeping with the gradualist approach, the Commission cautioned against a too-slow adoption of the *acquis communautaire* in certain areas, such as the free movement of people. Other areas of concern at the time were Slovenia's continued involvement in certain areas of the economy, slow privatization process and structural reform lags.

In 2003, Slovakia closed all the chapters of the *acquis* and completed negotiations for entry into the EU. President Drnovšek, Prime Minister Rop and foreign minister Rupel signed the treaty of accession between Slovenia and the EU on 16 April 2003 (Government Communication Office, 2010). Later that year, in November, Mr. Rop adopted the program of Slovenia's entry in the ERM II, a mandatory step on the path to the adoption of the euro (Government Communication Office, 2010).

The Slovenian Parliament ratified the treaty of accession of Slovenia to the EU in May 2004 (Government Communication Office, 2010). In line with the government's resolve to adopt the euro, it adopted a convergence program in mid-May as a key document for inclusion of Slovenia in the ERM II.

Parliamentary elections held in October 2004 brought in the former opposition Democratic Party (SDS) and established Janez Janša as Prime Minister until 2008. The 2004 elections represented the first time in over a decade that the Liberal Democracy of Slovenia lost control, ushering a new age of centre-right rule. The importance of the Liberal Democracy of Slovenia party is best

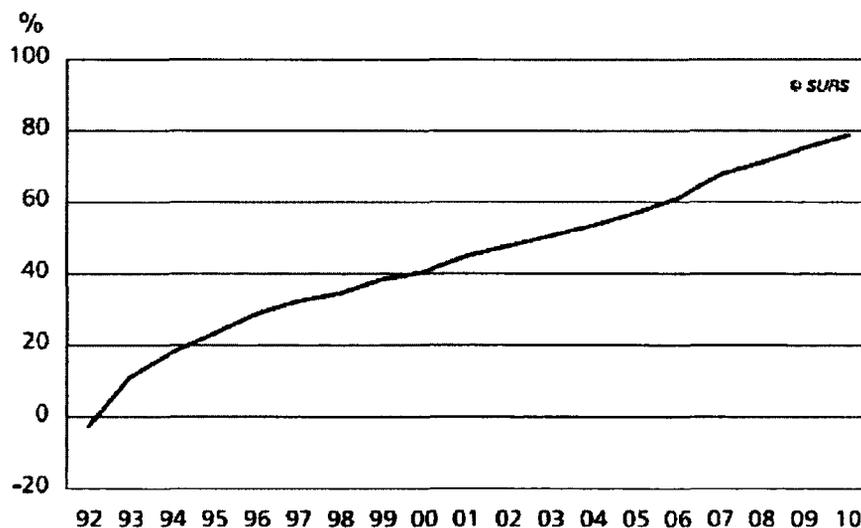
exemplified by the consolidation of democracy that led to Slovenia's entry into the EU. Conversely, it is important to note that Slovenia successfully completed its two-year in ERM II and adopted the euro under the Janša government.

3.3.2 Structural Labour Reforms

In Slovenia, the minimum wage is statutorily defined and is equal for all employees. It was introduced in 1995 with the agreement on the wage policy and other receipts of employees in the private sector, which was concluded as an annex to the social agreement for 1995 (Hren, et al., 2010). The minimum wage replaced the previously used guaranteed personal income or guaranteed wage (Hren, et al., 2010). Figure 11 shows that Slovenian wages have grown consistently since 1991.

Figure 11: Slovenian Wage Growth

Real growth of average net wage compared to 1991



Source: SURS

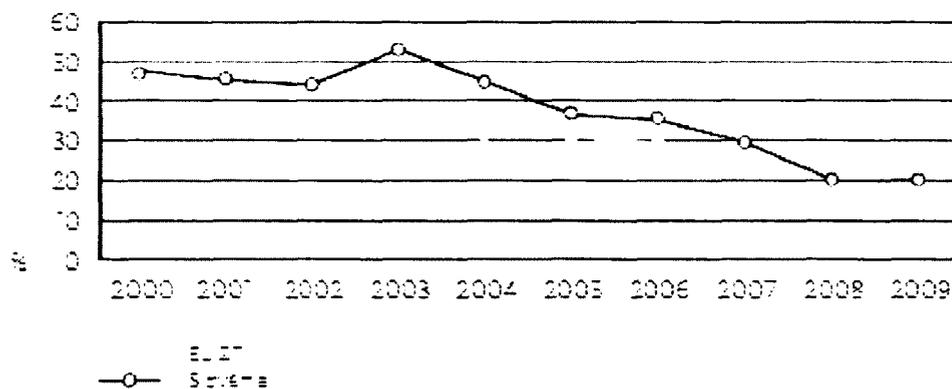
Source: Slovenian Statistical Office (2011)

During the 1990s, labour market policy relied heavily on expenditures on active measures. 'Employment subsidies, self-employment promotion programs, training and retraining of unemployed' were just some of the active labour market policy (ALMP) measures introduced (Bole, 2001, p. 269).

With youth unemployment a particularly serious problem, ALMP programs sought to transition youth into the labour market via a state-subsidized internship, starting in 1991 (Cesen, 2007). This program was 'abandoned in 1996 due to increasing burdens on the state', but reintroduced in 2005, though mainly to promote youth in the less developed regions of Slovenia (Cesen, 2007, p. 20).

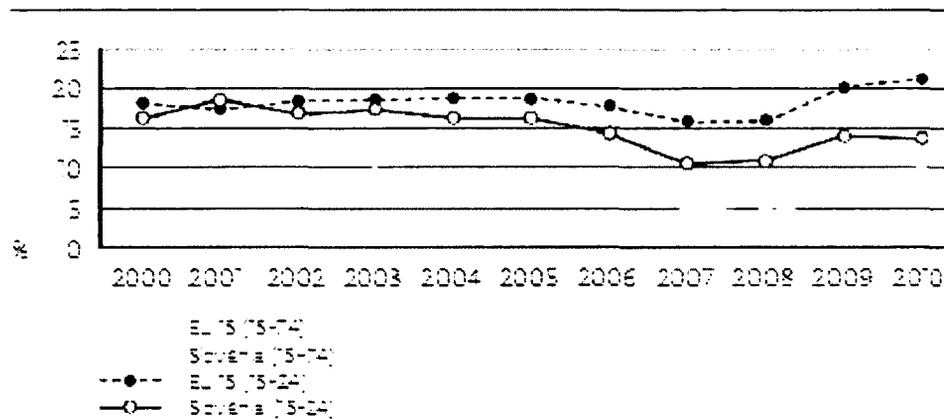
Figure 12 and Figure 13 confirm the trend of increasing flexibility in the youth labour market. Young people are increasingly finding themselves unemployed, while on the other hand the share of long-term unemployed has considerably declined over the past decade. One interpretation is that while it has become easier to hire and fire young people, youth are having an easier time finding new positions, since long-term unemployment has decreased. The prospects for finding employment can be seen to have improved.

Figure 12: Unemployment Rate, Slovenia vs. EU, 2000-2010



Source Lavric et al., (2010)

Figure 13: Share of Unemployed Slovenian Youth (15-24 years), Unemployed for 12 months or more

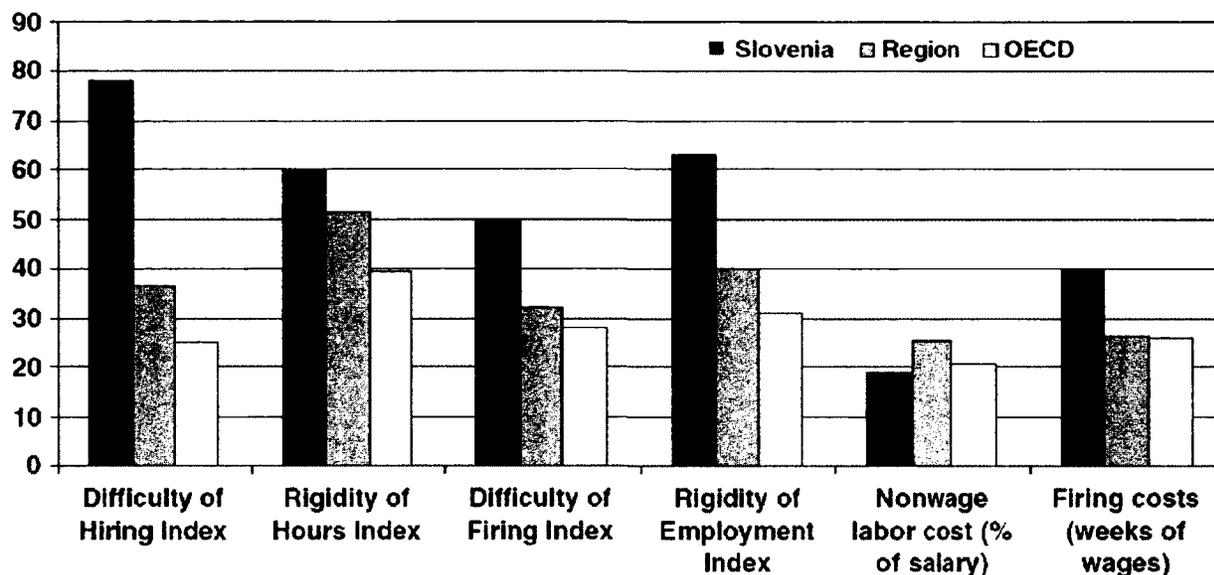


Source Lavric et al., (2010)

Before transition, unemployment cash benefits in Slovenia were very attractive. Benefits were 'high, long-term and pegged to the beneficiary's wage before becoming unemployed' (Bole, 2001, p. 271). Additionally, the government made pension system contributions for those registered as unemployed. At the beginning of transition, the benefits provided by the unemployment scheme remained unchanged, prompting scholars like Bole (2001) to link high benefits as a factor for unemployment remaining high well after transition. High unemployment placed an increasingly large burden on the government, and it was forced to adjust the eligibility conditions as well as the level of unemployment cash benefits.

Indeed, Figure 14 shows that as late as 2008, the employment rigidity remained higher in Slovenia when compared both against its central European neighbours and the OECD average. Hiring and firing difficulties (including costs associated with terminating a contract) contribute to the high unemployment and maintain an inflexible labour market.

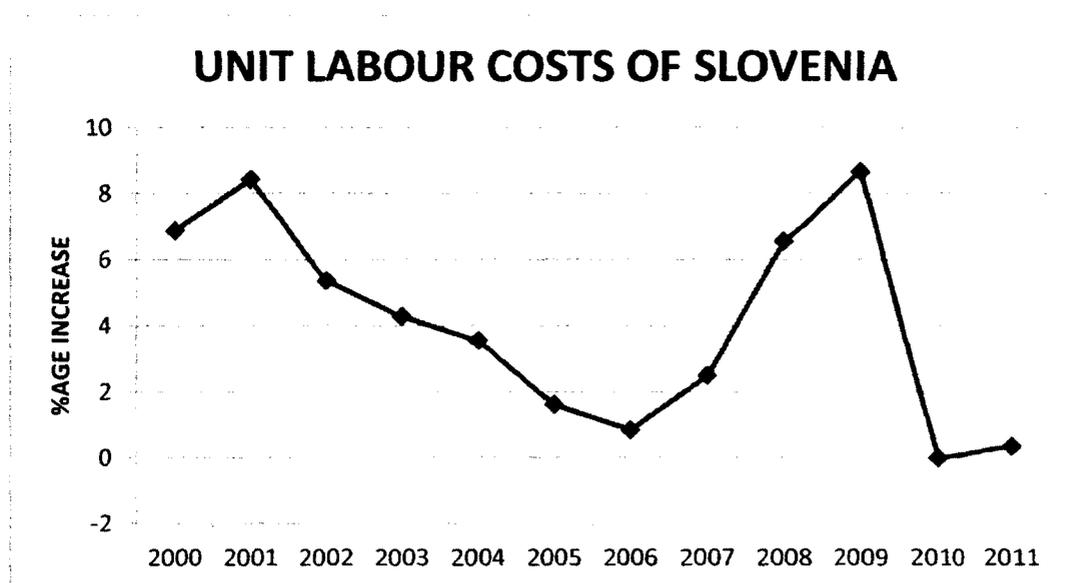
Figure 14: Ease of Doing Business in Slovenia, 2008



Source Lah et al., 2008

As depicted in Figure 15, ULCs in Slovenia had been decreased from 2001 to 2006. In 2006, though, as euro adoption was nearing, ULCs began to increase markedly, a cumulative 8% in three years. We know from Figure 14 that the labour market remained rigid while (based on Figure 12) unemployment decreased reflecting an increase in entrants in the labour market who used their strong position to demand higher wages (as evidenced by Figure 11) which translated to higher ULCs. This pattern continued through the beginning of the crisis in 2008, as most eastern European states were at first shielded from exposure, but was unsustainable by 2009 when contagion finally reached the region.

Figure 15: Unit Labour Costs Slovenia



Source OECD 2012

Labour Unions

In the 1980s, membership in trade unions was officially voluntary, but most workers were members and had dues deducted directly from their pay. Trade union officials usually were League of Communists of Yugoslavia (LCY) members and officials had few responsibilities thanks to the lack of distinction between employees and employers characteristic of the self-management system (Sabic & Brglez, 2002). Traditionally trade union officials opposed strikes; but in the late 1980s they modified this stand. In 1985 some union leaders broke tradition by suggesting that when 'workers' demands were justified and no other solution existed, the trade union should take the lead in organizing a strike' (Sabic & Brglez, 2002, p. 68).

In Slovenia, workers' councils have retained the influence they inherited from the Yugoslav system of self-management. In 1993 the system was transformed into a system of councils modeled on the example of German *Betriebsräte*. Works councils in Slovenia are very important entities for unions, because they grant access to union power at the firm levels (Buchen, 2005). Today, work councils exist in the majority of companies (Stanojević 2003).

The proportion of employees in trade unions is relatively high in Slovenia, at around 40% (ETUI, 2012). The Slovenian trade union landscape is fragmented consisting of seven union confederations as well as several autonomous unions (ETUI, 2012). The largest confederation is the Association of Free Trade Unions (ZSSS) which grew from the trade union structures that had existed before Slovenian independence in 1991.

Slovenian law allows unions to gain representative status, and, although this is not necessary in order to negotiate, representative unions have a number of advantages, such as only agreements reached by representative unions can be extended to those not directly involved in the negotiations (ETUI, 2012). In order to be judged representative, a union must, among other formal requirements, show that it is financially independent and has existed for at least six months (ETUI, 2012). A union confederation covering the whole country must also have 10% of the employees in membership in the industries, businesses or professions where it seeks to be representative (ETUI, 2012). A union operating on its own must have 15% of the employees in membership in an industry, business, profession or local area in order to be representative there (ETUI, 2012).

A law established in the final years of Yugoslav federalism concerning wage bargaining legislation made agreements between unions and employers compulsory. This, together with compulsory membership in the Chamber of Commerce, created a situation in which almost 100 % of the

workforce was covered by up to three collective agreements (European Industrial Relations Observatory, 2006). Amendments were made to this law in 2005 because compulsory agreements are against the guidelines of the EU (Skledar S. , 2006). The Law on Collective Agreements (LCA) introduced free and voluntary collective bargaining (European Industrial Relations Observatory, 2006). In preparing the law, the government adopted a consensual approach, which meant that the government, employers and trade unions had to agree on as many provisions of the draft LCA as possible before the government submitted it to the parliament for adoption (European Industrial Relations Observatory, 2006).

The group could not reach consensus on a number of issues, however. According to the EIRO (2006) some of the more contentious issues dealt with the hierarchy of the collective agreements, the procedure for signing up afterwards to a collective agreement and extending the validity of collective bargaining agreements

The EIRO (2006) reports this as a dividing issue. On one side there are those that regard the limited union reforms characteristic of Slovenia's gradualist model throughout transition and, on the other, those that cite the delay to underline how difficult it is to convince social organizations of the benefits of free collective bargaining.

Pensions

The Slovenian pension system is based on a state-funded pay-as-you-go (PAYG) model. Early retirement during transition caused a 'considerable reduction in the average age' of the newly retired (Bole, 2001, p. 273). As a result, total pension expenditures increased drastically. The generous benefits and qualifying criteria have resulted in Slovenia having one of the lowest effective retirement ages (Egoume-Bossogo & Tuladhar, 2006). To address the funding needs of

the pension system, the Slovene government pursued a reform in 1999 that extended the minimum number of years required to qualify for the full pension, increased the penalty for choosing to retire early and introduced a bonus for workers who choose to remain in the work force past the pensionable age (Egoume-Bossogo & Tuladhar, 2006). Following the 1999 reforms, workers could retire as early as age 58 if they met the minimum-pension-qualifying period of 40 years (38 for women). Otherwise, men could retire at age 63 and age 61 for women, after 20 years, or 65 and 63, respectively, after 15 years (Skledar Š. , 2007). To incentivize workers to remain in the workforce, the period for determining the pension rating base was increased from 10 to 18 years (Skledar Š. , 2007). The government has also tried to encourage supplementary private pension insurance as a means to alleviate some stress from the state-funded system, but this has yet to take off (Grobovsek & Kozamernik, 2009).

In March 2007, the IMF issued recommendations that strongly encouraged Slovenia to undertake further pension reforms in an effort to bolster its sustainability (IMF, 2007). However, the landscape for reform at the time seemed bleak, with authorities informing the IMF delegation that systemic reform would not be politically feasible in the short term due 'strong opposition from trade unions, who perceive pension privatization as undermining the public social insurance system' (Ottawa, 2007, p. 1).

Though Slovenia may have been able to put off reforms while it was the fastest-growing Eurozone member in 2007, with its economy expanding by 6.9% , it has been badly hit by the global crisis, with its economy contracting by 8% in 2009, and can no longer dispute the need for reform (Novak, 2012).

3.3.3 Taxation

Slovenia's tax system was formed in the 1990s, as part of the new set of legal documents of the independent republic.

A new personal income tax and corporate income tax were outlined in the tax code (Majcen et al., 2009). During the 1990s, few changes were introduced to both taxes, whereas in 2004, new laws on personal income and corporate income were passed. In 2006, new tax codes for personal and corporate income tax were introduced, which have been in effect since January 2007, the same year Slovenia adopted the euro (Majcen et al., 2009).

The need for frequent tax reforms came from increasing pressure from citizens, business and external actors (EU, IMF) to address the high taxation and opaque and complex tax codes. As an example, prior to the 2006 reform, wages were taxed first at almost 40% to cover social security contributions, and additionally taxed between 0 and 14.8% as part of the progressive payroll tax (Majcen & et al., *The Income Tax Reform in Slovenia: Should the Flat Tax Have Prevailed?*, 2009).

Debate emerged in 2006 about introducing a flat tax rate, similar to the one introduced in Slovakia and was even proposed by the government with its reform proposal (The Economist Intelligence Unit, 2007). This idea was met with such a negative response from the Slovenian labour unions that the flat tax idea was cast aside in favour of a new three-tax-bracket personal income tax code and some changes to the corporate income tax code (The Economist, 2007). Specifically, the 2007 tax reform reduced to three the number of brackets for personal income tax (The Economist Intelligence Unit, 2007). It also reduced the highest marginal personal income tax rate from 50% to 41%, taxed interest, dividends and capital gains at 20% and reduced the statutory corporate income

tax rate from 25% to 20% (Majcen & et al., *The Income Tax Reform in Slovenia: Should the Flat Tax Have Prevailed?*, 2009).

A sales tax of 20% on consumer products and 10% on services was replaced as of 1 July 1999 with Slovenia's VAT (The Economist, 2007). The VAT was introduced at a standard rate of 19% and a reduced rate of 7.5% (The Economist, 2007). On 1 January 2002 the standard rate was augmented to 20% and the reduced rate was increased to 8.5%, where it has remained unchanged since 2005 (Majcen & et al., *The Income Tax Reform in Slovenia: Should the Flat Tax Have Prevailed?*, 2009). The reduced rate applies to food, medicines and agricultural products (Majcen & et al., *The Income Tax Reform in Slovenia: Should the Flat Tax Have Prevailed?*, 2009). Exports, insurance, banking and financial services are exempt.

Taxation changes reflect Slovenia's particular implementation of gradualism. For instance, the 2007 tax code outlines the gradual abolition of the payroll tax over a number of years, a direct contrast to the overnight change strategy pursued in Slovakia with the replacement of the flat tax rate.

3.3.4 Concluding remarks

Throughout Slovenia's preparations for inclusion in the EMU, economic policies were focused on preserving macroeconomic stability including (relative) fiscal and balance of payments equilibrium. This focus was made possible by Slovenia's gradualist approach to transition, which implies a successive and long-term process of structural reforms (instead of the 'big bang' approach of quick and radical economic reforms). Though this approach is often criticized by international institutions, in the specific case of Slovenia, gradualism played to the country's strengths and allowed it to reach its goal in both EU and euro accession. Moreover, the pursuit of

EMU and adoption of the euro in Slovenia was backed by the most important political parties and also received support from the public. In short, euro adoption was an overall national project which united Slovenians rather than dividing them, as had been the case with some other major national economic programs.

3.4 Slovakia

Overview

Sharon Fisher (2006) argues that governments in East Central Europe were given two choices: they could either launch a transition to democracy and a market economy that would lead to a return to Europe or they could move back towards a regime based on authoritarianism, using cronyism and corruption to gain and maintain influence and power.

The state of confusion and uncertainty in Eastern Europe at the time added to the difficulty for countries to make the choice between more Europe or more of the same. The 1990s were basically characterized by political and economic upheaval which left the elites of Central and Eastern Europe the guardians of a large amount of power. It also left them with the opportunity to deal with the vast amount of property which had fallen into state hands, a veritable breeding ground for the spreading of corruption vis-à-vis questionable privatization deals and/or through the skimming of funds from assets that remained under the ownership of the state.

3.4.1 Political forces

Kevin Deegan-Krause (2005) argues for the pivotal role of elites in shaping public opinion in Slovakia. The influence of 'Europeanist' elites in Slovakia waxed and waned at the beginning of the 1990s. The term 'elites' refers to leading Slovak economists, journalists and intellectuals that

rallied behind reformist politicians, like Dzurinda, in the name of smooth transformation and integration. Support from elites helped win over the public and created an atmosphere of consensus, all of which was made possible thanks to civil society organizations (mainly, NGOs) funded by the international community (Gallina, 2007).

1990s

The first multiparty elections were held in Czechoslovakia in 1990, ‘giving way to the defeat of communist forces and the establish[ment] of the basic structures of democratic institutions and a market economy’ (Fisher, *Political Change in Post-Communist Slovakia and Croatia: From Nationalist to Europeanist*, 2006, p. 24). When in 1992 elections were held again, growing tensions with the Czechs regarding the form of state arrangement and economic reforms in the Slovak part of Czechoslovakia summed the 1992 elections as a sort of referendum on the future of Czechoslovakia and on economic reform. With the election of Klaus as Czech prime minister in 1992, the Slovak population found themselves in a difficult position. Though efforts had been undertaken to establish more equality between the two people, the Czech regime change delivered a less accommodating message to the Slovak people: either they accept the federation as it was or declare full independence. The Slovak population, angry that their government was not sufficiently representing what they felt were national interests, accepted the new state with resignation. In 1993, the reorganization of the two new states, Slovakia and the Czech Republic, proceeded peacefully with foreign aid. Mečiar was named the prime minister in Slovakia and the parliament shortly thereafter approved the new constitution. The dissolution, known as the ‘velvet divorce’, was relatively smooth in large part due to private talks between Mečiar and Klaus.

Despite Europeanist efforts following the break from Czechoslovakia, during the early 1990s, nationalist elites still reigned in Slovakia.

Vladimir Mečiar led his party, the Movement for a Democratic Slovakia (HZDS). The HZDS chose to ignore in large part the recommendations of western governments and international institutions. This hostile response, as has been argued by Fisher (2006) was largely coloured by the idea that accession to the EU seemed far-away and so there was no real incentive for the leadership to relinquish power to authorities in Brussels. Mečiar was briefly unseated as prime minister in March 1994 by the parliament³², with opposition parties creating a new government under Jozef Moravčík. This lasted only until elections in that same year returned him and his HDZS party (in coalition with the Slovak National Party) to power.

The turning point, perhaps, came in 1997 when many of the CEECs were invited to join NATO and formally start accession negotiations with the EU. Slovakia did not receive an invitation. The frustration and perhaps embarrassment of being left behind while all its neighbours moved forward, combined with the growing prevalence of corruption and abuse of government powers, confirmed to the population that their ruling elite was not acting in the country's best interest. The time was ripe for the opposition, the Europeanists, to move in and sweep elections in 1998. The results of the 1998 elections were clear. The people had spoken and no longer were willing to accept the cronyism and corruption. The ruling party had lost touch with the voters and could no longer find the salient issues to lure them back. The need for nationalistic movement no longer existed, taking with it the party that had championed for it.

Europeanists reappeared as the dominant political force. Mikuláš Dzurinda's Slovak Democratic Coalition (SDK) won the parliamentary elections in 1998 and took a clear lead over Mečiar's nationalist HZDS party. The HZDS never really recovered, despite 'trying to change its image by

³² For more on this, see: <http://www.slovakia.org/history-topics>

renaming itself, in 2000, the People's Party-Movement for a Democratic Slovakia' (Fisher, Political Change in Post-Communist Slovakia and Croatia: From Nationalist to Europeanist, 2006, p. 19).

Dzurinda's SDK government preferred quick economic reforms and an antinationalist approach, favouring more autonomy to address the specifics of the Slovak situations, with emphasis on economic reforms. Under Dzurinda, Slovakia was re-aligned to pursue integration processes which improved the country's relations, both with the European Union and trans-Atlantic economic and political structures. The success of the reforms put through by Dzurinda's cabinet during its first mandate was reflected in Slovakia's entry into the OECD in September 2000, completion of accession negotiations with the European Union and the entry of major investors into the Slovak market (Kosta & Bednarik, Slovakia, 2008).

The new Dzurinda government acknowledged the harmful effects of corruption and placed anticorruption high on the official agenda. Key milestones to support the administration's desire to address corruption included: participation by the Prime Minister in a public conference on corruption; the formation of an Anticorruption Steering Committee under the leadership of the Deputy Prime Minister; and the first drafting of the National Program for the Fight Against Corruption in 1999 (World Bank and USAID, 2000). Nevertheless, a tolerance for accepting bribes persisted in a system where corruption is greatly facilitated by slow service delivery, which in turn is frequently generated by bureaucratic rules that hinder an institution's ability to deliver services quickly.

The results of the 2000 World Bank and USAID survey, requested by the Slovak government, indicated that corruption was perceived to be widespread and especially problematic in health, justice, the National Property Fund, customs, police, and ministries. Moreover, many citizens

believed that corruption was more widespread than it was in 1990. The results of the surveys show clearly that corruption is associated with bureaucracy, with firms and households paying bribes to speed the processes along and that the lack of clear guidelines for the acceptance of gifts leaves officials with no guidance for acceptable behaviour.

2000s onwards

In January 2000³³, Dzurinda founded a new political party, the Slovak Democratic and Christian Union (SDKU). The electorate supported the reformist course of the Dzurinda government, as evidenced by the 2002 general election which handed Dzurinda his second mandate (The Economist, 2003). The second Dzurinda government (2002-2006) reduced the budget deficit, paving the way towards Eurozone adoption, introduced a 19% flat tax and attracted foreign direct investors which propelled economic growth. The new, simplified flat tax combined with the governments' adoption of EU competition laws increased the functioning of free and efficient markets and led to an export boom (predominantly led by the electronics and automobile sectors) (Gould, Slovakia's Neoliberal Churn: The Political Economy of the Fico Government, 2006-2008, 2009). Though Dzurinda oversaw Slovakia's entrance into the EU and was committed to preparing the economy for euro adoption, its coalition suffered from a number of political scandals which led to early elections.

Dzurinda's party was defeated by Robert Fico's Social Democracy (Smer) party in the 2006 parliamentary election. Smer, a left-wing populist party, campaigned against Slovakia's successful flat tax and favoured more government intervention in the economy (The Economist, 2006). Smer formed a coalition government with two nationalist parties, HZDS and the Slovak National Party

³³ Slovak diplomatic cable <http://dazzlepod.com/cable/04BRATISLAVA161/>

(SNS), the latter being regarded as an extremist nationalist party by the Party of European Socialists of the European Parliament.

Despite campaigning against the reforms pursued by the previous Dzurinda government, Fico presented no new economic vision and inherited economic success which lasted from 2006-2008. While the economy was indeed strong, the lack of progress in competition policy or infrastructure have been heavily criticized by many, the European Bank for Reconstruction and Development (ERBD) among them (Gould, Slovakia's Neoliberal Churn: The Political Economy of the Fico Government, 2006-2008, 2009).

Fico publically questioned the value of the euro but options were few as the previous Dzurinda government had moved Slovakia into ERM II in November 2005 (Johnson, 2008). Though provisions exist for leaving ERM II, exit is not without consequences. Participation in ERM II signals to the markets that a country is stable and has its fiscal and monetary house in order. When Fico implied that Slovakia might consider postponing its planned 2009 euro adoption for fiscal reasons, currency speculators began to attack the Slovak crown, 'forcing a costly intervention by the Slovak National Bank' (Gould, Slovakia's Neoliberal Churn: The Political Economy of the Fico Government, 2006-2008, 2009, p. 13), forcing Fico to reiterate Slovakia's commitment to the 2009 target date (Johnson, 2008). In any case, Slovakia's fast-growing economy brought about inflation risk which could only be managed by restrictive monetary policy. Despite earlier misgivings and hesitations about the euro and even promises to halt or reverse reforms, Fico must have realized that 'it was either Maastricht today or some form of slow growth and uber-Maastricht tomorrow' (Gould, Slovakia's Neoliberal Churn: The Political Economy of the Fico Government, 2006-2008, 2009, p. 14).

The Fico government's renewed commitment to fiscal discipline was evident in the 2007 budget that registered a low deficit at 2.9% of GDP and low inflation at 2.8% (Gould, Slovakia's Neoliberal Churn: The Political Economy of the Fico Government, 2006-2008, 2009). Strong and continued growth in the economy also made it possible for the government to adhere to the ERM II criteria without having to drastically reduce government expenditures. While presence in ERM II and the ensuing fiscal discipline did not allow Fico to fulfill his campaign promises of expansive social programs, it did grant the government credibility since it was not required to cut government programs or reduce the government-employed work force.

On the 10th anniversary of the euro, January 1, 2009, Slovakia adopted the euro. The President of the European Commission, José Manuel Barroso stated:

'On this tenth anniversary of the euro, I congratulate Slovakia and warmly welcome all its citizens to the euro area. The euro will help Slovakia to take part in, and benefit from, Europe's collective effort to recover from the current economic crisis. By joining the euro area, Slovakia has enhanced its long-term potential to create growth and jobs and keep inflation under control. But the euro is more than just money. On this historic New Year's Day, Slovakia is a powerful symbol of economic and political progress and of European integration' (Commission, 2009, p. 1).

Corruption has been a major issue in Slovakia for some time. Corruption claims against the center-right parties contributed to the 2006 change in government (Sustainable Governance Indicators, 2009). The fight against corruption, however, did not feature in the Fico government's program and no official government strategy in the field existed (Sustainable Governance Indicators, 2009). As stressed by Hoppe and Schmidt-Hebbel (2009) the Fico government also abolished the special

court and the special prosecutor's office for corruption cases which had been established by the previous government in order to improve enforcement. Party cronyism and clientelism flourished. In a number of cases, public subsidies, state contracts or emission rights went to firms close to representatives of the governing coalition (Sustainable Governance Indicators, 2009). Under Fico, government interference with the courts' independence increased (Sustainable Governance Indicators, 2009). This ranged from public comments on the performance of particular courts and justices, attempts to directly influence individual court decisions, to the initiation of disciplinary proceedings against and the suspension of inconvenient justices (Sustainable Governance Indicators, 2009). In a poll by the Institute for Public Affairs (IVO) (2008), 42% of the respondents said the level of corruption had worsened and another 45% did not see any progress. According to the poll, corruption was the field in which citizens were the most critical of the Fico government.

3.4.2 Structural Labour Reforms

During the early transition period, labour market policy in Slovakia was characterized by the tendency to 'finance passive measures and by insignificant expenditures on active measures' (Kosta & Bednarik, Slovakia, 2008, p. 341). The payment of unemployment benefits was tightened in the late 1990s and coincided with a pronounced emphasis on active labour market policy (ALMP) following the reforms in 1997 (Kosta & Bednarik, Slovakia, 2008).

Slovakian unemployment insurance was reformed in the late 1990s in an attempt to address the high unemployment rate (Kosta & Bednarik, Slovakia, 2008). Entitlement to unemployment benefits became more restricted after the reform. Older workers which had benefitted more under the old system saw that advantage eroded as the duration of benefit payments was made 'uniform for all unemployed people' (Kosta & Bednarik, Slovakia, 2008, p. 343). At the end of 2000, the

share of those receiving unemployment benefits had declined to 18% from 82% in 1991; by the end of 2005 it had declined to a mere 8.8% of the unemployed (Kosta & Bednarik, Slovakia, 2008). While these numbers seem encouraging, this was mainly due to higher standards for qualifying for benefits, as high unemployment continued to plague the Slovakian labour market.

Slovakia showed 'significant economic growth and relatively low inflation in the second half of the 1990s' but high unemployment persisted (Fisher, *Political Change in Post-Communist Slovakia and Croatia: From Nationalist to Europeanist*, 2006, p. 84). The ruling parties exchanged favours with big business, via privatization, to the detriment of small and medium enterprises (SMEs) and the middle class. Trade unions and the media brought some attention to the growing disparity, and citizens, fed up with the contradictions between political rhetoric and actual practices, began to look to alternative parties and away from HZDS.

The second half of the 1990s was met with increasing criticism of the ruling party's approach to privatization. Trade unions, which had initially been in support of the privatization methods of Mečiar's 1994-98 cabinet as it promised to promote employee privatization, soon grew disenchanted.

As political strikes were prohibited by labour laws, Slovaks were, at first, reluctant to partake in protests and demonstrations but as the 1998 elections approached, interest began to materialize (Fisher, *Political Change in Post-Communist Slovakia and Croatia: From Nationalist to Europeanist*, 2006). Slovaks were not willing to accept the excuses of the Mečiar government any longer and sought change.

The Dzurinda governments of 1998 and 2002 were hailed in the international press. *The Economist* (2006) claimed that Dzurinda, 'made Slovakia a reform star of central Europe, with a flat tax, labour deregulation and a solid pension system.'

Labour market reforms were undertaken by the Dzurinda government, extending to the liberalization of labour law, cuts in unemployment benefits, the introduction of welfare-to-work programs and individualized job counseling (OECD, 2007). 2003 saw changes to labour laws, essentially establishing a business-friendly environment to spur on investment. Hiring and firing of workers became much easier and unions were marginalized by the dissolution of the Tripartite Act in 2004, which basically removed a formal channel through which union partners sought to influence economic policy (Gould, *Slovakia's Neoliberal Churn: The Political Economy of the Fico Government, 2006-2008, 2009*).

The Dzurinda government kept spending on active labour market policy relatively low, especially in the eastern regions where the unemployment rate is the highest and long-term unemployment looms large (Sustainable Governance Indicators, 2009). Little was done to address the growing disparity between the eastern and western regions, and the problem continues to grow.

The high unemployment which haunted the previous decade was still proving problematic.

Unemployment increased to almost 20% under Dzurinda's first government, and was still at 12% when he left office, one of the highest rates in Europe.

The Fico government proceeded in the opposite direction on labour policies, namely toward re-regulation of the labour market. Minimum wage laws were reformed at the end of 2007 to reflect advances in the economy as a result of EU participation (Gould, *Slovakia's Neoliberal Churn: The Political Economy of the Fico Government, 2006-2008, 2009*).

The Fico government 'reinstated the tripartite act in 2006' and in 2007 introduced a new labour code (Gould, *Slovakia's Neoliberal Churn: The Political Economy of the Fico Government, 2006-2008, 2009*, p. 18). Gould (2009, p. 18) outlines that the new law limited the use of independent contractors, reduced compulsory and overall limits of overtime hours, prevented the repeat use of temporary workers (to encourage long-term employment), raised the notice and compensation periods for fired workers and lowered the threshold for workers who can be fired without cause from 20 hours a week to 15. These changes enabled labour unions to regain some of the power they had previously lost under the Dzurinda government. Importantly, workers also gained the right to employer compensation for time off due to union obligations and labour representatives gained the right to be consulted on employee performance standards. Though unions were still relatively weak vis-à-vis union engagement in other EU countries, the 2007 reforms granted them a new platform from which to be heard. The introduction of the new labour laws has succeeded in bringing Slovakian work standards and employee protection closer to European standards.

In 2009, Slovakia was the 'most export-dependent post-communist country in post-communist Europe' (Gould, *Slovakia's Neoliberal Churn: The Political Economy of the Fico Government, 2006-2008, 2009*, p. 19). The requirement for an agile and skilled work force that could perform well across multiple sectors and transition seamlessly was needed. However, since the accession to the Eurozone, the labour policy in Slovakia has not addressed the lack of labour mobility in much detail. Despite the advances, the labour law reforms of 2007 did not address the lack of geographical mobility within Slovakia, nor did it touch on the huge disparity in unemployment in the west (as low as 1.8%) versus the east (as high as 28%) (Gould, *Slovakia's Neoliberal Churn: The Political Economy of the Fico Government, 2006-2008, 2009*). The lack of labour mobility

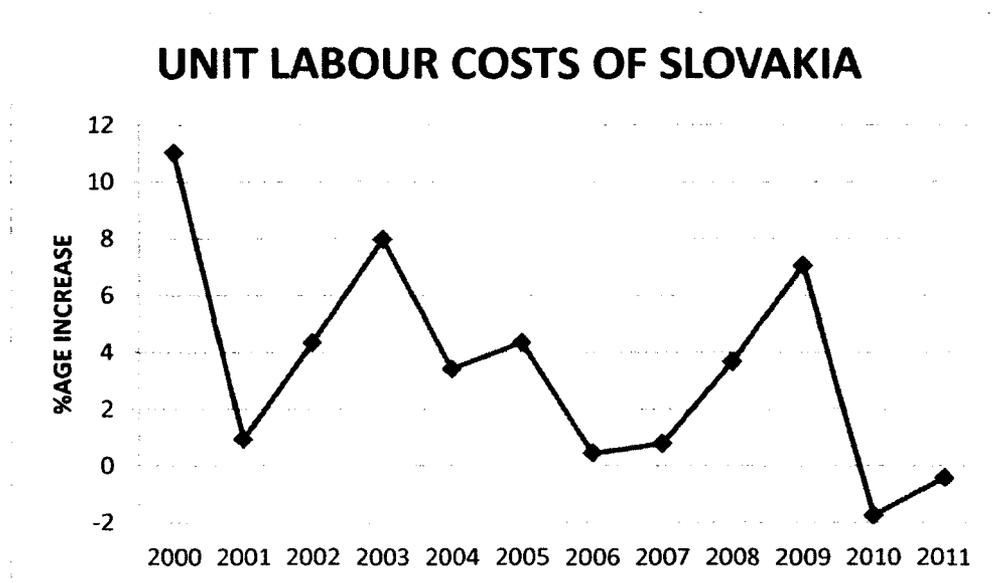
reflects underlying structural changes that still and pressingly require attention. ALMPs must be coordinated in order to address the regional imbalances and sector inflexibilities.

External agencies, looking to the balance of progress in labour reforms, were hesitant about the lack of wage flexibility, especially as euro adoption drew near. The IMF warned that increased wage flexibility would be crucial once the National Bank of Slovakia (NBS) lost its control over monetary policy and labour would be left to deal with the realignments (IMF, 2008). The IMF further advocated that wage negotiations occur at the enterprise level and that increases in workers income be directly tied to productivity gains. Moreover, both the IMF and the OECD were concerned about the use of raising the minimum wage in order to satisfy a ‘living minimum’ (Gould, Slovakia's Neoliberal Churn: The Political Economy of the Fico Government, 2006-2008, 2009, p. 20). Instead, the IMF advocated for providing low wage workers with an earned income credit that would ‘raise their income to the living minimum, encouraging people to take jobs that would let them qualify for the credit and encourage higher employment’ in areas where unemployment was highest and wages lowest (Gould, Slovakia's Neoliberal Churn: The Political Economy of the Fico Government, 2006-2008, 2009, p. 21). Much progress remains to be made, especially as concerns the growing disparity between eastern and western regions of Slovakia.

ULCs in Slovakia have been relatively volatile, increasing and decreasing rapidly.

Figure 16 shows that though volatility persists, a decrease relative to the 2000 value can be noted and has been sustained, even when ULCs have increased. We can also note a delay in adjusting ULCs for the financial-turned-economic crisis, with ULCs coming down only in 2010.

Figure 16: Unit Labour Costs Slovakia



Source OECD data (2012)

Labour Unions

With transition, Slovakia abandoned its centralized system of wage-setting for a collective bargaining system in the private sector (Kosta & Bednarik, Slovakia, 2008). Bargaining at the national level is carried out by the tripartite Council for Economic and Social Accord, which is made up of participants from trade unions, employers' associations and the government. National level bargaining which sets out minimum wage increases in each sector, is conducted infrequently, with wage bargaining taking place mostly at the company or industry level (Kosta & Bednarik, Slovakia, 2008).

Labour union participation has been declining since Slovakia's independence when workforce participation was 100% (EIRO, 2010). An OECD (2004) report states that Slovakian unionization

decreased from 57% in 1995 to 36% in 2000, to 30% in 2004 and to about 20% in 2009. An explanation for the lack of labour union participation is that by 2004, collective agreements covered about half of all workers (Kosta & Bednarik, Slovakia, 2008). Though an EIRO (2009) report notes that that number has since increased to 35% of the workforce, the high employment protection in large firms must provide workers with a sense of security, thus not needing to seek labour union protection.

Moreover, the 2007 Labour Code assured more generous severance packages for workers, also serving to decrease employees' need to rely on a union as dialogue with the government is open. The new Labour Code also set out new conditions for renewing temporary contracts, imposing a limit of one contract renewal (Kosta & Bednarik, Slovakia, 2008).

Pensions

The pension system before 1989 reflected the political system of the time. Pensions under the state socialist regime were paid out from the state budget (Lesay, 2006). The level of pension depended only 'very moderately' on level of income (Lesay, 2006, p. 9). Pensions were egalitarian and the system was based on redistribution and solidarity. The pension system before the reform was to a great extent a successor of the socialist pension system.

The pre-reform system was institutionally governed by the Social Insurance Agency, launched under the Mečiar government in 1995. There were two types of pension systems in place. The first was a 'mandatory, publicly-managed defined-benefit (DB)' social security system (Lesay, 2006, p. 10). It was financed on a pay-as-you-go (PAYG) basis (Gould, Slovakia's Neoliberal Churn: The Political Economy of the Fico Government, 2006-2008, 2009). The second option was a voluntary supplementary pension insurance system (Lesay, 2006).

The Dzurinda government introduced a three-pillar pension system in accordance with World Bank guidelines in 2004 (Sustainable Governance Indicators, 2009). This refers to a pension system divided into public pensions (pillar one), occupational pensions (pillar two) and personal pensions (pillar three).

The transformation to the pillar system brought about changes. Under the first pillar, pension entitlement was changed with the retirement age being raised to 62 years for both sexes. Changes for men came into force in 2006, while for women, it will enter into force in 2015 (Lesay, 2006).

The second pillar was a new addition to the Slovak pension system. The pillar is formed by 'redirecting part of contributions to personal pension accounts managed by pension management companies (PMCs)' (Lesay, 2006, p. 13). These private companies seek to increase the value of savings by investing through a selected pension fund. Restrictions do apply which prohibit pensioners or people with fewer than 10 years to retirement age from participation. People who decide to join the second pillar will get their pension from two sources-half the contribution from the first pillar plus what remains in the second pillar account at the retirement (Lesay, 2006).

The third pillar represents voluntary supplementary pension insurance.

Reforms also made it mandatory for young people and new labour market entrants to put 9% of their earnings into both the first and second pillars. Despite the higher risk and compulsory participation for younger workers, the second pillar was a 'political success attracting close to a third of population' (Gould, Slovakia's Neoliberal Churn: The Political Economy of the Fico Government, 2006-2008, 2009, p. 21).

The reforms by the Dzurinda government were aimed at improving the system's sustainability by highlighting the contribution-benefit link. Nevertheless, the first pillar has and continues to suffer from a shortfall in financing.

Fico campaigned against the private pension system. Once in government, the Fico administration added to the already-burdened first pillar's fiscal problems by introducing a 'Christmas bonus for retirees' (Lesay, 2006, p. 38). The government has tried to discourage Slovaks away from the second pillar. Breaking with the original rules, the second pillar was opened up twice in 2008 to encourage private savers to return their private savings to the state via the first pillar (Sustainable Governance Indicators, 2009). On those occasions, the National Bank of Slovakia rejected claims by the government and it publicly emphasized the sound supervision and the high efficiency of the second pillar (Sustainable Governance Indicators, 2009).

In 2009, the Fico government introduced regulations that limited both the potential risks and benefits from participating in the second pillar (Gould, Slovakia's Neoliberal Churn: The Political Economy of the Fico Government, 2006-2008, 2009, p. 24). Confusingly, the government introduced legislation compelling fund managers to guarantee 100% of pensioners' savings, a move which stands to provide even less incentive for savers to leave the second pillar now that risk has been reduced. In keeping with the reduction in the maximum fee pension funds can charge their companies instituted in 2009, it would appear that the government is banking on the refusal of foreign funds to continue to provide services when restricted to pursuing investments in low risk, low growth assets (Gould, Slovakia's Neoliberal Churn: The Political Economy of the Fico Government, 2006-2008, 2009).

Risks from capital market fluctuations, fund mismanagement and inadequate state guarantees pose serious risks and rippling social impacts, reiterating the need for labour market reforms and the tackling of unemployment.

3.4.3 Taxation

The most fundamental changes to the tax code took place in January 2004. The 19% value-added tax (VAT) received much attention in the press. Coming into effect January 1, 2004, the Dzurinda government replaced the complex tax code it had inherited from the former Czechoslovakia. The pre-2004 tax code consisted of five tax brackets ranging from 10% to 38%; 90 different exemptions; 19 unique sources of tax-free income; 66 items that were themselves tax-exempt; and an additional 27 items that carried their own particular tax rates. A split VAT taxed 'some items and services at 14%, others at 20%', lacking evident logic or reason (Gould, Slovakia's Neoliberal Churn: The Political Economy of the Fico Government, 2006-2008, 2009, p. 15). To add to the confusion, tax laws were often changed. The 2004 reform sought to alleviate the confusion by setting personal income tax, corporate income tax and the VAT all at 19%.

The government's goal, as stated on the Ministry of Finance's site was:

'[T]o transform the Slovak tax system into the most competitive one in the entire EU and OECD area. By a competitive tax system, the government does not merely mean low degree of taxation – far from it. The Slovak tax system should be competitive mainly because of the unusually high degree of its efficiency, transparency and non-distortiveness' (The Fundamental Tax Reform, December 2004, 2005).

The reform had many implications beyond the new 19% flat tax rate. Three broad objectives were laid out. First, the creation of a business and investment friendly environment for both individuals and companies was stressed. Second, the elimination of existing weaknesses and distortionary effects of the tax law was ordered. Third, tax fairness was sought by a revision that all types and amounts of income would be taxed equally.

To achieve the three objectives the tax burden was shifted from direct toward indirect taxes, from taxing production toward taxing consumption. Low standard tax rates were introduced and all exceptions, exemptions and special regimes were eliminated, in order to achieve its stated aim of tax transparency. The flat tax rate on personal income was introduced, which got rid of the tax bracket system. Care was taken to eliminate, where possible, the double taxation of income (The Fundamental Tax Reform, December 2004, 2005).

In fact, virtually all tax deductions and exemptions that were originally intended to achieve non-fiscal policy goals were replaced by targeted measures in the relevant policy areas (social insurance, pension and healthcare). Exceptions and exemptions, including tax holidays, tax breaks, individual tax bases, and special tax rates were eliminated from the corporate tax law as well (The Fundamental Tax Reform, December 2004, 2005). Lump-sum taxes for entrepreneurs were cancelled- a particularly acute problem in Slovakia where it was common for salaried workers to declare themselves self-employed- and a regime of deductible lump-sum expenditures was introduced (The Economist, 2005).

The clarity and simplicity of the new tax law established a higher degree of transparency and aided in the development of a business-friendly environment. Additionally, this change in the tax code

addressed one of the main business barriers identified in Slovakia by business surveys – the excessive complexity and frequent changes in the tax law.

Moreover, the low corporate tax rates and high transparency of corporate and investment tax laws ‘sharply reduced the scope for tax evasion and tax avoidance, and led to increased tax collection’ (Gould, *Slovakia's Neoliberal Churn: The Political Economy of the Fico Government, 2006-2008, 2009*, p. 15).

The new legislation eliminated the 21 different types of taxation of direct income that were in force in Slovakia, including five different personal income tax rates (10%, 20%, 28%, 35% and 38%) replacing it with the single 19% flat-tax (The Fundamental Tax Reform, December 2004, 2005).

The flat-tax retained some of the progressive nature of effective tax rates of the pre-2004 system. It states that all personal income of up to 1.6 times the poverty line is exempt from taxation (The Fundamental Tax Reform, December 2004, 2005). Individuals earning below that threshold would not be taxed on their income, therefore mitigating the negative impact on low-income earners, having a small impact on the middle-income earners, and the greatest impact on the highest-earning individuals. Policy-makers and analysts pointed out that this single marginal tax rate would encourage individuals who had previously evaded the tax system, due to incomprehension or belief of unfair taxation laws, to participate (The Economist, 2005). The Slovakian Ministry of Finance foresaw increased labour productivity both in the short and long term, as it encouraged higher work effort at any given point in time, as well more investment in human capital, as a secondary benefit (The Fundamental Tax Reform, December 2004, 2005).

The corporate tax rate was reduced from its 25% to the new 19% level (The Fundamental Tax Reform, December 2004, 2005). The new system ensured the singular taxing of investment and

capital gains income- this occurring as it is transferred from the corporate to the personal level. Another benefit of the 2004 tax code change was the elimination of dividend taxation.

The standard VAT rate in the pre-2004 tax code was 20%, with a reduced rate of 14%. The reform eliminated the reduced VAT replacing it with the 19% rate for all goods and services. This generated increased tax revenues and eliminated economic distortions and inefficiencies associated with taxing the consumption of various goods differently (The Fundamental Tax Reform, December 2004, 2005).

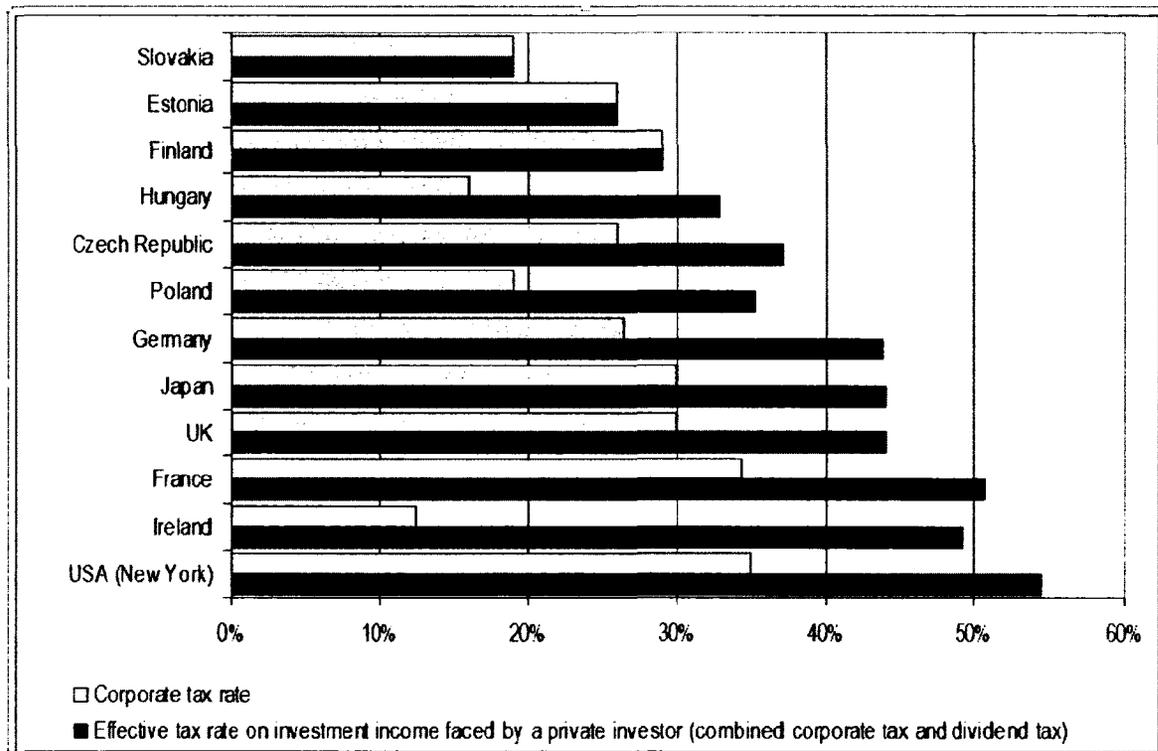
Reduced VAT rates were being used to justify non-fiscal arguments. Reduced VAT rates were supposed to lead toward the achievement of non-fiscal policy goals. They were expected to generate lower prices, leading to better access by low income groups to basic food and other selected goods, or increased consumption of goods deemed to be socially desirable (The Fundamental Tax Reform, December 2004, 2005). Evidence of such pattern-changing behaviour via reduced-VAT was not found so the Dzurinda government replaced the underperforming policy instrument with targeted instruments, as mentioned before, in relevant policy areas, such as social policy and health care.

The tax reform also increased excise duty rates on mineral oils, tobacco and tobacco products, and beer (The Fundamental Tax Reform, December 2004, 2005). The increased excise taxes on tobacco products led to the early harmonization of Slovak tax law with EU regulations.

The extensive reform of the tax code validated the governments' hopes and received praise from economists to executives (The Economist, 2005). In fact, as Figure 17 shows, Slovakia achieved one of the most competitive tax systems in both the EU and the OECD as a result of the reform.

Figure 17 compares the Slovakian business-related tax rate to that of its neighbours and a selection of OECD participants, demonstrating the competitiveness which Slovakia has gained and which explains the country’s ability to attract foreign investment.

Figure 17: Comparison of Tax Rates Faced by Investors, Slovakia vs. Selected Countries



Source: Government of Slovakia (2008)

The Smer government was not entirely satisfied with the reformed tax code. Fico criticized the reforms, saying that they went against ‘the social character of Slovakia³⁴’ by ‘under-taxing Slovakia’s wealthiest and over-taxing its poor consumers’ (Gould, Slovakia’s Neoliberal Churn: The Political Economy of the Fico Government, 2006-2008, 2009, p. 16). During his campaign, Fico promised to lower the VAT, but left the system largely untouched and confined himself to minor changes, because the system has received much international acclaim and has turned out to be quite popular in Slovakia (Slovakia’s Reform Status- Taxes, 2011). In the spring of 2009, the Fico government made progress in the efficiency with which VAT refunds for corporations are ‘processed and received’ (Gould, Slovakia’s Neoliberal Churn: The Political Economy of the Fico Government, 2006-2008, 2009, p. 16). This was well received and continues to be a popular measure amongst the business community, as it enhances the image of Slovakia as business-friendly.

3.4.4 Concluding Remarks

The Slovakian economy is an inviting destination for business with a simple flat tax rate and a labour market that is not limited by over-intrusive labour unions. More must be done to address the lack of labour mobility and growing regional disparity. The Fico government’s efforts at dissuading private pension funds may prove misguided as the population ages and the financial burden increases on the state, especially as public finances are increasingly scrutinized thanks to the on-going financial crisis. Additionally, steps must be taken to address the corruption problems

³⁴Diplomatic cable from American Embassy in Bratislava: <http://dazzlepod.com/cable/06BRATISLAVA457/>

which have become a mainstay of the political landscape and undermine the citizens' trust in their political leaders.

4 Cases Comparison

Figure 18 summarizes the effectiveness of the reforms in Spain, Greece, Slovenia and Slovakia.

Figure 18: Comparison of Case Studies

COMPARISON OF CASE STUDIES								
	EU ENTRY	EURO	POLITICAL FORCES	LABOUR POLICIES			TAX POLICES	
				UCL	LABOUR UNIONS	PENSIONS	Tax rates	Enforce.
SPAIN	1986	1999	Very committed to euro adoption; Corruption not relevant factor	Gradual increase over time; adapted once crisis hit	Strong post-transition; Influence decreased as business interests strengthened	Quite generous	Progressive income, business friendly	Acceptable
GREECE	1981	2001	Actions reflected commitment to euro but rhetoric lacked; Corruption highly relevant	High volatility Adapted late to crisis	Strong	Very generous	Progressive; complicated	Unacceptable Highly susceptible to corruption
SLOVENIA	2004	2007	Committed to euro, but at own pace; Corruption not relevant factor	Moderate increase over time. adapted late to crisis	Weak	Moderately generous	Progressive	Acceptable

SLOVAKIA	2004	2009	Committed to euro adoption as soon as feasible; Corruption needs to be addressed	High volatility adapted late to crisis	Weak	Moderately generous	Business friendly	Acceptable
----------	------	------	----------------------------------------------------------------------------------	----------------------------------------	------	---------------------	-------------------	------------

Political

We observe that in all of the countries analyzed the governments that formed immediately after the transition were motivated and committed to seeing their respective country join the European Union.

In Greece, Spain and Slovakia two interesting patterns can be outlined. The first is that despite periodic changes in governing political party, any party that came to power continued with the reforms that its predecessor had begun. In Slovenia this is less apparent because of the speed with which reforms were undertaken. The various governing parties tended to maintain the gradualist approach, with the exception of the decision to adopt the euro.

The second pattern is that socialist parties across the four case study countries campaigned on agendas that promised to see the reforms halted, and undone where possible, but once they were elected, abandoned their anti-Europe and anti-euro rhetoric. This second pattern was not as present in Slovenia as a result of their commitment to gradualism.

Once in power, socialist governments embraced reforms citing that their main concern was modernizing and improving their country and the lives of its citizens. Indeed, the parties went as far as redefining their political goals to reflect the need for EU membership, and later euro

inclusion. The euro, it was seen, promised to help enhance the economic welfare of the country which would in turn enhance the opportunities of citizens.

Labour

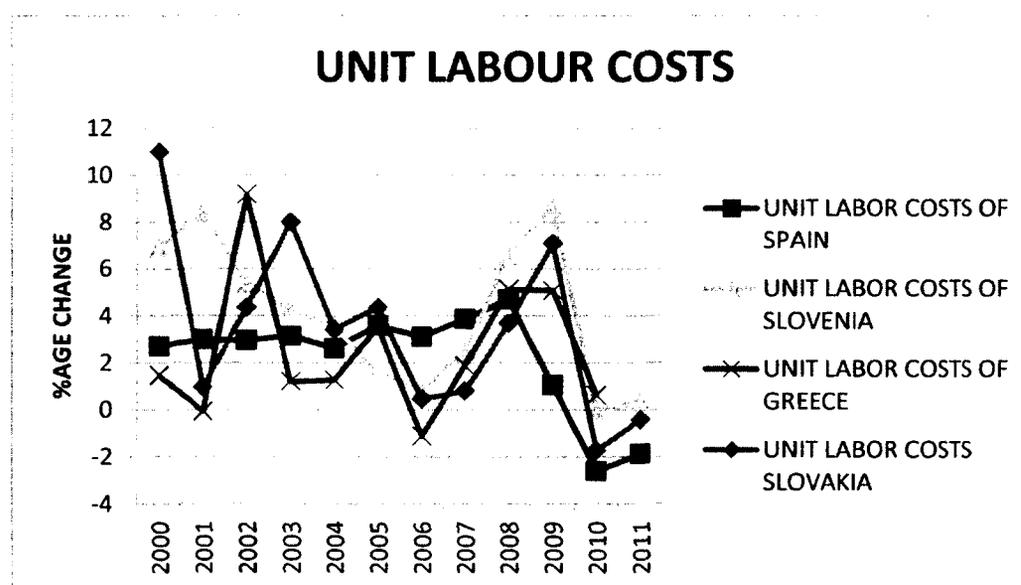
All of the countries examined underwent various reforms aimed at the labour market and its policies.

Labour unions are present in all countries and had a significant role in the economies of Spain and Greece. Labour unions in Spain were instrumental in its transition to democracy, much like in Greece, but declined in importance as business interests gained power. As a result, Spain was able to institute deeper reforms. In Greece, the size of the government has ensured that unions maintain a stronghold on the economy and any related decision. In turn, this has led to suspended economic activity whenever a government has had the courage to suggest reform, leading the government to sacrifice reform progress in the name of economic prosperity. Both Slovenia and Slovakia are small countries in terms of population which influences the need for union representation. Slovenia's unions are fairly fragmented so their ability to consolidate to oppose the government is limited, but so is the need for union action thanks to the gradualist path chosen by Slovenia's governments. Slovakia, too, has had a limited use for labour unions. This is reflected by the low union participation rates amongst employees and the preference for collective bargaining in the private sector. The Labour Code in Slovakia, reformed in 2007 by the Smer government, has adapted the provisions to reflect a code that is more reassuring to the Slovakian workers.

We note that of the four case countries, Spain has had the most moderate increases in ULCs and was the most responsive to adjusting ULCs once the crisis hit. Greece has shown volatility in its ULCs similar to that of the new member states, which can suggest a lack of maturity in the labour

market. Moreover, Greece was late to respond to the crisis, with ULCs decreasing only once the crisis had become very pronounced in Europe. This can represent a lack of flexibility in the labour market. Slovenia's ULC fluctuations are more moderate than Slovakia's. In Slovenia, ULCs decreased until about 2006, the year preceding its euro adoption, then increased until 2009 when the crisis forced a sudden adjustment. Slovakia, on the other hand, has followed a path similar to that of Greece, where volatility is more pronounced in its ULC changes. We can compare ULCs across all four case study countries in Figure 19.

Figure 19: ULC Comparison, Spain, Greece, Slovenia and Slovakia



Source OECD data (2012)

Pension reform was a contentious issue across all four countries. Reforms were undertaken to redefine the qualifying criteria and benefits. In all cases, this resulted in a longer qualifying period and a reduction in the benefits received by pensioners. What is clear is that neither the older nor the newer member states managed to undertake the radical changes necessary to move towards a more sustainable pension system. Greece, until recently imposed reforms, was infamous for the generosity of its pension, both regarding qualifying age and average pension allotment. Though

pension reforms were routinely introduced, the structural deficiencies of the system were left untouched for fear of the backlash from the unions. Spain managed to implement somewhat deeper cuts to the pension system while the conservatives were in power (1996-2002). They were able to do this thanks to the support they had from business organizations and the happy coincidence of weakened labour unions at the time. Slovenia managed to push through reforms which raised the average qualifying period for pensioners, but little else as unions have held back much-needed pension reforms. In Slovakia, the entire pension system was re-organized into a three-pillar system which was aimed at improving the system's sustainability by highlighting the contribution-benefit link. Nevertheless, insufficient reforms have meant that the first pillar, the public pensions, continues to suffer from a shortfall of financing.

Taxation

Trends regarding taxation across the countries were varied. This is a result of many things; not least the idea that as monetary policy autonomy has been completely relinquished greater importance has been placed upon fiscal policies to compensate for a perceived lack of sovereignty.

Reforms in all countries were aimed at simplifying and clarifying the tax code in an effort to encourage increased compliance from taxpayers and increased tax receipts for the government.

Greece, though in dire need, has done the least to address or enhance transparency of its tax code. This in turn has continued to support an environment of high-tax evasion that is commonly acknowledged by politicians but rarely addressed by new policy. Spain was more successful in addressing the shortcomings of its tax code. Personal and corporate income tax rates were harmonized to European standards, with increases explained as necessary for the continued functionality of a generous welfare state. Slovakia was particularly motivated in this respect and

introduced a 19% flat tax rate. Slovenia was not as daring, opting instead for a reduction of brackets in the personal income tax code and minimal changes to corporate rates. The gradual changes to the tax system are further evidence of Slovenia's preference for slow-and-steady reform.

Spain and Slovakia pursued measures to create a more business-friendly environment, the former through a reduction in corporate taxes and the latter through a one-tax-fits-all policy. From this perspective, it can be said that encouraging and promoting business through the tax regime is a not priority in Greece or Slovenia.

While we observe that all countries introduced a VAT in line with the EU-wide guidelines that have replaced their various sales taxes, the rates are not harmonized.

What can be discerned from this analysis is that the countries generally moved in the same direction, with the occasional difference in Slovenia as a result of its moderated approach. It does not seem that the newer member states, Slovakia and Slovenia, appreciated enough the lack of reforms in older member states, Greece and Spain, to reflect on the state of their own reforms.

The political perspective shows convergence across the countries, the result of the politicians' uniform will to see their country part of a greater unity. That politicians were willing to overlook their own ideology in favour of the greater good speaks volumes to the often-questioned credibility of the European Union and the euro.

Labour reforms seem to have had the least progress, encountering the greatest and most persistent obstacles. Though the need is imminent in all countries to address the issue of flexibility in the labour market, and more specifically unemployment, the decision on how to move forward

remains stalled as the various stakeholders-employees, employers, unions, the government-continue debating.

Some convergence is observed in taxation, though only briefly and mainly a result of EU demands. As the VAT is necessary for EU membership, we note that it has been introduced in all countries, replacing various sales taxes in its wake. Other taxes such as income and corporate taxes cannot, at this time, be seen as converging. The direction of tax rates are reflected in the interests of the respective governments. In the member states where promoting business has been important, reductions were effectuated, while in member states which were concerned with providing a generous welfare state the opposite held true.

This analysis has shown that Greece has consistently underperformed the other three case study countries on all reform issues. It is telling that Greece has been most affected since the crisis took hold in Europe. The lack of political will and unity to effectuate reforms and address its serious corruption problem has exacerbated its budgetary problems, leading to two bail-outs with a possible third on the way. Spain has so far been able to manage its economic position, thanks to having undertaken wider reforms, but with the economic crisis still strong, it must continue to act and implement further reforms, especially in the labour market. Slovenia and Slovakia have the chance to learn from Greece's mistakes. Slovenia must move past its gradualist tendencies and concentrate on dealing with the rigidities of its labour market. Slovakia must re-assess its policies regarding the sustainability of its pension system. Both Slovenia and Slovakia can take advantage of being new, fairly small Eurozone states to implement the essential reforms needed to avoid future economic peril.

Summary and Conclusion

This thesis has examined four Eurozone member states, Spain, Greece, Slovenia and Slovakia across three perspectives on their paths to adopting the euro. The three perspectives, political forces, labour and taxation policies, encompass important reforms.

The political analysis traced the political changes in each country from their transition from authoritarian state to democracy and onwards to the adoption of the euro. The structural labour reforms examined what was done to increase labour market flexibility and what role unions played in any transformations undertaken. Taxation reforms analyzed the evolution of the structure of the tax code as indicated by changes to income, corporate and value-added taxation.

These three perspectives provided a narrative of how each member state managed its path towards the euro. We observed that where political will was strong and not limited by corruption greater reforms were undertaken. We noted that labour reforms have been the most difficult and contentious to implement. We saw that taxation policies can be useful in attracting business but that policies show no real convergence across the case studies.

We saw that depth of reform, or lack thereof, can seriously affect a country, as in the case of Greece. Though Greece has become the model for failed reform, the fear of contagion is not unfounded. We are beginning to see similar problems with Spain, whose debt level is alarmingly high, and it is not unrealistic to imagine Slovenia and Slovakia succumbing to the same fate as the crisis has led to large increases in their debt to GDP ratios. In part thanks to the reforms that Spain did carry out, it has so far managed to maintain the confidence of investors in international money markets, as reflected by its last two debt auctions. This has bought the country some time to launch

a series of drastic, overdue reforms. These reforms are being touted as inevitable by the ruling PP government, signaling that ignoring the need to reform does not make the need disappear.

The importance of this comparative study lies in its applicability by new member states of the European Union as they contemplate their own path towards adopting the euro. As new member states do not have the option to opt out of adopting the euro, care should be taken to analyze the mistakes committed by their fellow member states and identify how those policy errors can be avoided in their respective cases. As the new member states integrate, they will experience a period of rapid growth. Attention must be paid during this time to ensure that reforms are not overlooked during prosperity and growth. If new member states do overlook implementing reforms, then they may put themselves at risk of following the same path as Spain and especially Greece.

The economic crisis has not spared any country, but the damage to countries that had undergone serious structural reforms before the crisis has been contained and does not threaten the economic viability as we see in Greece, and may yet see in Spain. Slovenia and Slovakia, though insulated from initial shocks, are not beyond the reach of the systemic economic crisis. The only insurance against contagion is to create a flexible and resilient economy that will be able to absorb shocks and adapt. Real reform, especially of the labour market, must lead the new era.

Further Research

Though much research has been conducted on the economic theories behind the political choice to push for a common currency, and equally, studies have been carried out on individual member states' paths towards the euro, additional research must now be done at a comparative level. These countries have not chosen to enter the European Union and then the euro by chance. They assessed that they identified with the values and direction laid out by the European project and that they were suitable for, and wanted to partake in, such a union. This must mean that on many levels, member states share similarities, be they social, economic, legislative, cultural, historical or identity. If this holds true, then some of their journeys must have been similar.

One area of study, of particular interest to the author, is that of assessing the similarities of Mediterranean countries and peripheral countries. Have countries such as Portugal, Spain, Italy and Greece had the same success and challenges? Is this due to something innate in the Mediterranean culture? Do the new member states of Romania and Bulgaria exhibit the same characteristics? If so, can anything be done to tackle the problems before they arise? If not, do they share similarities with other old member states?

Can similarities and contrasts be drawn across member states that joined the EU and the euro at the same time? What impact do exogenous events occurring in the greater global economy have, on the one hand, on the choice to pursue reforms in a member state, and on the other, the success of the reforms undertaken to address a particular problem.

Additionally, research matching up new member states to older member states could prove useful for forecasting purposes and for avoiding repeating the same mistakes.

Bibliography

Afonso , A., & Furceri, D. (2009). Sectoral Business Cycle Synchronization in the European Union. *Economics Bulletin*, 2996-3014.

Diamandouros, N. P., & Gunther, R. (2001). *Parties, Politics, and Democracy in the New Southern Europe*. Maryland: The Johns Hopkins University Press.

González-Páramo, J. (2005). *The reform of the Stability and Growth Pact: an assessment*. Frankfurt: European Central Bank.

Sustainable Governance Indicators. (2009). *Slovakia Report 2009*. Gütersloh: Bertelsmann Stiftung.

The Fundamental Tax Reform, December 2004. (2005, 05 27). Retrieved 01 15, 2012, from Ministry of Finance of the Slovak Republic: <http://www.finance.gov.sk/en/Default.aspx?CatID=118>

Institutional and economic framework of the euro. (2006, August 16). Retrieved 06 08, 2011, from Europa: http://europa.eu/legislation_summaries/economic_and_monetary_affairs/institutional_and_economic_framework/l25061_en.htm

The new VAT rates from July 1. (2010, June 24). *Mandata (in Greek)*.

Greek civil servants face the austerity axe. (2011, October 3). *euronews*.

-
- Slovakia's Reform Status- Taxes.* (2011). Retrieved February 6, 2012, from Sustainable Governance Indicators : http://www.sgi-network.org/index.php?page=countries_status&country=svk&pointer=8#point_8
- Aghion, P., & Blanchard, O. (1994). On the Speed of Transition in Central Europe. *National Bureau of Economic Research.*
- Albonetti, A. (2005). *L' Italia, La Politica Estera E L'unita Dell'Europa.* Rome: Lavoro.
- Alexakis, p., & Apergis, N. (1994). Monetary policy in Greece: the impact of EC membership. In *EC Membership Evaluated* (pp. 74-95). New York: St. Martin's Press Inc.
- Alfaro, L., Dessain, V., & Damgaard Jensen, A. (2007, April 30). All Eyes on Slovakia's Flat Tax. (M. Lagace, Interviewer) Bratislava: Institute of European Studies and International Relations, Comenius University.
- Aza, A. (2000). Adolfo Suárez's Stewardship of the Transition- a memoir. In M. Threlfall, *Consensus Politics in Spain: Insider Perspectives* (pp. 27-41). Portland: Intellect Books.
- Baldinger, & Breuss. (2006). Country Size and the Gains from Trade Bloc Enlargement: an Empirical Assessment for the European Community. *Review of International Economics*, 615-631.
- Balogová, B., & Liptáková, J. (2009, January 12). 2008 Racks Up Some Controversial Laws. *The Slovak Spectator.*
- Barry, F. (2001). Fiscal Policy in EMU. In E. P. (eds.), *European Monetary Integration* (pp. 119-131). Aldershot: Edward Elgar.

BBC. (2011, October 19). Greek government austerity measures. *BBC*.

BBC. (2012, April 19). Timeline: The unfolding eurozone crisis. *BBC*.

Bindi, F. (2011). *Italy and the European Union*. Washington: The Brookings Institution.

Blavoukos, S., & Pagoulatos, G. (2008). Fiscal Adjustment in Southern Europe: the Limits of EMU Conditionality. *Journal of Public Policy*, 229-253.

Bole, V. (2001). Fiscal Impulse of Transition: The Case of Slovenia. In M. I. Blejer, & M. Skreb, *Transition: The First Decade* (pp. 259-292). Cambridge: The MIT Press.

Bonin et al. (1999). *Beyond the Toledo Agreement*. Barcelona: Facultat d'Economia, Universitat de Barcelona.

Bradsher, K. (1989, June 20). Peseta Jumps as Spain Joins Currency System. *The New York Times*.

Brown, B. (2004). *Euro on Trial: To Reform or to split up?* New York: Palgrave Macmillan.

Broz, T. (2005). The Theory of Optimum Currency Areas: A Literature Review. *Privredna kretanja i ekonomska politika*, 53-78.

Buchen, C. (2005). East European Antipodes: Varieties of Capitalism in Estonia and Slovenia. *Varieties of Capitalism in Post-Communist Countries* (pp. 1-39). Wiesbaden: Paisley University.

Butti, M., & Sapir, A. (1998). *Economic Policy in EMU*. Oxford: Clarendon Press.

-
- Callejo, J., Meseguer, P., & Moron, R. (2008). El mantenimiento de la pauta tradicional. In C. Prieto, R. Ramos, & J. Callejo, *Nuevos tiempos del trabajo* (pp. 185-229). Madrid: Centro de Investigaciones Sociologicas.
- Carr, R. (1982). *Oxford History of Modern Europe: Spain, 1808-1975*. Oxford: Clarendon Press.
- Casella, A. (1995). Large Countries, Small Countries, and the Enlargement of Trade Blocs. *European Economic Review*, 389–415.
- Ca'Zorzi, M., & Schnatz, B. (2007). *Explaining and forecasting euro area exports: Which competitiveness indicator performs best?* Frankfurt: European Central Bank.
- Centre for Economic Policy Research. (1985). *Greece Under PASOK: New Lessons for Development Policy?* London: Centre for Economic Policy Research.
- Cesen, T. (2007). YOUTH EMPLOYMENT IN SLOVENIA. *EIPF Conference on Youth Employment* (pp. 15-22). Emerging Issues Policy Forum (EIPF).
- Clark, R. P. (1979). *The Basques, the Franco years and beyond*. Reno: University of Nevada Press.
- Closa, C., & Heywood, P. M. (2004). *Spain and the European Union*. New York: Palgrave Macmillan.
- Cobham, D., & Zis, G. (1999). *From EMS to EMU: 1979 to 1999 and Beyond*. New York: St. Martin's Press Inc.
- Colombo, A., & Ronzitti, N. (2008). *L'Italia e la politica internazionale*. Bologna: Il Mulino.

-
- Comin, F. (2006). *Reaching a Political Consensus for Tax Reform in Spain*. Atlanta: George State University.
- Comín, F. (2007). Reaching a Political Consensus: The Moncloa Pacts, Joining the European Union, and the Rest of the Journey. In J. Martínez-Vázquez, & J. Sanz-Sanz, *Fiscal Reform in Spain: Accomplishments and Challenges* (pp. 8-59). Northampton: Edward Elgar.
- Commission of the European Communities. (1990). *One Market, One Money*. Brussels: EC.
- Commission, E. (2009, 1 1). Slovakia adopted euro today. Brussels. Retrieved from EU.
- Costa, C., & De Grauwe, P. (1999). EMU and the Need for Further Economic. In W. M. (ed.), *Economic Policy in the European Union*. Cheltenham: Edward Elgar.
- Costa, C., & De Grauwe, P. (1999). EMU and the Need for Further Economic Integration. In W. Meeusen, *Economic policy in the European Union* (pp. 27-49). Northampton: Edward Elgar Publishing, Inc.
- Davaki, K., & Mossialos, E. (1994). Health Policies. In P. Kazakos, & P. Ioakimidis, *Greece and EC Membership Evaluated* (pp. 260-279). New York: St. Martin's Press.
- De Grauwe, P. (2003). In S. S. (ed.), *Euro Adoption in Central and Eastern Europe: Opportunities and Challenges* (pp. 41-58). Washington: International Monetary Fund.
- De Grauwe, P. (2009). The Fragility of the Eurozone's Institutions. *Open Economic Review*, 167-174.
- Debeljak, A. (2011, December 20). THE VIEW FROM UNION STREET: FROM YUGOSLAVIA TO THE EUROPEAN UNION. *Citizenship in Southeast Europe*.
-

-
- DeSantis, R. (2007). The EMU: A Challenging Goal for the "New" Member States of European Union? *LA COMUNITA' INTERNAZIONALE*, 1-11.
- Duval, & Elmeskov. (2006). *The Effects of EMU on Structural Reforms in Labour and Product Markets*. Frankfurt: European Central Bank.
- Dyson, K., Underhill, G. R., Wessels, W., Linsenmann, I., Gamble, A., Kelly, G., et al. (2002). *European States and the Euro*. New York: Oxford University Press.
- Easson, A. (2004). *Tax Incentives for Foreign Direct Investment*. The Hague: Kluwer Law International.
- Economic and Financial Affairs DG. (2009). *Economic Crisis in Europe: Causes, Consequences and Responses*. Luxembourg: European Commission.
- Ecorys Nederland BV. (2011). *Study on the cost competitiveness of European industry in the globalisation era - empirical evidence on the basis of relative unit labour costs (ULC) at sectoral level*. Cambridge: DG Enterprise.
- Egoume-Bossogo, P., & Tuladhar, A. (2006). *Tax, Welfare, and Pension Reforms in*. New York: IMF.
- EIRO. (2010). *Trade union strategies to recruit new groups of workers – Slovakia*. Bratislava: EIRO.
- El Mundo. (1997, January 6). El PP recorta distancias con el PSOE por las buenas expectativas económicas para 1997. *El Mundo*.

EL PAÍS. (1986, January 18). El paro registrado a finales de 1985 alcanzó a 2.731.505 personas.

EL PAÍS.

Encarnación, O. G. (2008). *Spanish Politics: Democracy after dictatorship*. Cambridge: Polity Press.

Ethier, D. (1997). *Economic Adjustment in New Democracies*. New York: St. Martin's Press, Inc.

Ethier, D. (1997). *The Economic Context of Democratic Transitions*. London: Macmillan Press Ltd.

ETUI. (2012). *Trade Unions*. Retrieved February 8, 2012, from Worker Participation, European Union: <http://www.worker-participation.eu/National-Industrial-Relations/Countries/Slovenia/Trade-Union>

Eurofund. (2009, August 14). *Industrial Relations Spain: Reforma Laboural de 1994*. Retrieved February 20, 2012, from Eurofund: <http://www.eurofound.europa.eu/emire/SPAIN/LABOURLEGISLATIONREFORMOF1994-ES.htm>

euronews. (2011, October 3). Greek civil servants face the austerity axe. *Euronews* .

European Central Bank. (2011). *Economic and Monetary Union (EMU)*. Frankfurt: ECB.

European Central Bank. (2011). *The Public Sector Pay Gap in a Selection of Euro Area Countries*. Frankfurt: European Central Bank.

European Commission. (2009). *European Competitiveness Report*. Brussels: European Commission.

European Industrial Relations Observatory. (2006). *Law on collective agreements adopted*.

European Industrial Relations Observatory.

Eurostat. (2011). *Taxation trends in the European Union: Greece*. Brussels: Eurostat.

Fidrmuc, J. (1999). Trade Diversion in 'Left-Outs' in Eastward Enlargement of the European Union: The Case of Slovakia. *Europe-Asia Studies*, 633-645.

Fink-Hafner, D. (1996). Organized Interests as Policy Actors in Slovenia. In Agh, & I. (eds.), *Parliaments and Organized Interests: The Second Steps* (pp. 222-240). Budapest: Hungarian Centre for Democracy Studies.

Fisher, S. (2006). *Political Change in Post-Communist Slovakia and Croatia: From Nationalist to Europeanist*. New York: Palgrave MacMillan.

Fisher, S. (2010). Civil Society and the EU Enlargement Process: Lessons from Slovakia and Croatia. *The Second Meeting of the Working Group on the Western Balkans: Enhancing Civil Society Participation in EU Enlargement*.

Flemr, J. (2009, January 02). Czechs take over EU helm, slovakia embraces euro; former czechoslovakia takes historic step. *Times-Colonist*, p. A.10.

Gallina, N. (2007). Political Elites in Eastern Central Europe: Paving the Way for 'Negative Europeanisation?'. *Contemporary European Studies*, 75-91.

Gomez, R. P. (2007). The Evolving Role of the Corporate Income Tax. In J. Martinez-Vazquez, & F. Sanz-Sanz, *Fiscal Reform in Spain* (pp. 208-241). Northampton: Edward Elgar Publishing.

Gould, J. A. (2009). *Slovakia's Neoliberal Churn: The Political Economy of the Fico Government, 2006-2008*. Bratislava: Institute of European Studies and International Relations, Comenius University.

Gould, J. A. (2009). *Slovakia's Neoliberal Churn: The Political Economy of the Fico Government, 2006-2008*. *Institute of European Studies and International Relations, Comenius University*, 1-31.

Government Communication Office. (2010). *1991*. Retrieved February 2012, from 20 Years of Independence: Republic of Slovenia: <http://www.twenty.si/first-20-years/91/>

Grobovsek, J., & Kozamernik, D. (2009). Reforming the Slovenian Pension System: Some Guidelines and Intergenerational Distribution Issues. In L. M. Robert Holzmann, *Pension Reform in Southeastern Europe: Linking to Labour and Financial Market Reform* (p. 381). Washington: World Bank Publications.

GRReporter. (2011, November 12). Greeks believe their tax system is complex, inefficient, non-transparent and socially unjust. *GR Reporter: News from Greece*.

Gunther, R., Montero, J. R., & Botella, J. (2004). *Democracy in modern Spain*. Princeton: Yale University Press.

Haffner et al. (2005). European Integration, Liberalization and Labour Market Performance. In Bertola (eds) et al. , *Welfare and Employment in an United EuropeB* (pp. 147-237). Cambridge: MIT Press.

Hastedt, G. P. (2004). *Encyclopedia of American Foreign Policy*. New York: Facts On File Inc.

-
- Herz, B., & Kotios, A. (2000). Coming Home to Europe:Greece and the Euro. *Intereconomics*, 170-179.
- Holman, O. (1996). *EC Expansion and the Transnationalization of Spain*. New York: Routledge.
- Hope, K. (2010, April 16). Greek taxpayers sense evasion crackdown. *Financial Times*.
- Hosli, M. O. (2005). *The Euro: A Concise Introduction to European Monetary INtegration*. Boulder: Lynne Reinner Publishers.
- Hren, K., Cirjakovic, J., Korenic, R., Kralj, A., Peceli, S., Repovz Grabnar, I., et al. (2010). *To Slovenia For Its 20th Birthday*. Ljubljana: Statistical Office of the Republic of Slovenia.
- Hughes, J., Sasse, G., & Gordon, C. (2004). *Europeanization and Regionalization in the EU's Enlargement to Central and Eastern Europe*. New York: Palgrave MacMillan.
- IMF. (2007). *Republic of Slovenia: Selected Issues*. Washington: IMF.
- IMF. (2007, March 13). *Slovak Republic-2007 Article IV Consultation Discussions, Preliminary Conclusions of the Mission*. Retrieved September 30, 2011, from International Monetary Fund: <http://www.imf.org/external/np/ms/2007/031307.htm>
- IMF. (2012). *IMF Country Report No. 12/57*. Washington: International Monetary Fund.
- Instituto Nacional de Estadística (INE). (2011). *Encuesta de Población Activa (EPA)* . Madrid: Instituto Nacional de Estadística (INE).
- Issing, O. (2008). *The Birth of the Euro*. Cambridge: Cambridge University Press.
- Jackson, T. (1997, 02 03). German business leaders doubt 1999 start date. *Financial Times*, p. 01.
-

- Jiménez, F. (2004). The Politics of Scandal in Spain. *American Behavioral Scientist*, 1099-1121.
- Johnson, J. (2008). The remains of conditionality: The Faltering Enlargement of the eurozone. *Journal of European Public Policy*, 826-841.
- Jonsson, A. (2006). Changing Concepts of Rights in Post-Communist Societies. In S. P. Ramet, & D. Fink-Hafner, *Democratic Transition in Slovenia: Value Transformation, Education, and Media*. Texas A&M University Press.
- Kalaitzidis, A. (2010). *Europe's Greece*. New York: Palgrave Macmillan.
- Kaplanoglou, G., & Newbery, D. M. (2002). *Indirect Taxation in Greece: Evaluation and Possible Reform*. Munich: Center for Economic Studies & Ifo Institute for Economic Research.
- Koch, M. (2004). Labour Market Regulation after Fordism. In P. Littlewood, I. Glorieux, & I. Jonsson, *The Future of Work in Europe* (pp. 11-31). Burlington: Ashgate.
- Konstantopoulou, Z. (2003). Grèce / Greece. *Revue internationale de droit pénal*, 255-289.
- Kosta, J., & Bednarik, R. (2008). Slovakia. In I. Kogen , M. Gebel, & C. Noelke, *Europe enlarged: A handbook of education, labour and welfare regimes in Central and Eastern Europe*. Bristol: The Policy Press.
- Kosta, J., & Bednarik, R. (2008). Slovakia. In M. G. Irena Kogan, *Europe Enlarged: A handbook of education, labour and welfare regimes in Central and Eastern Europe* (pp. 323-351). Bristol: The Policy Press.
- Lavdas, K. A. (1997). *The Europeanization of Greece*. New York: St. Martin's Press.
-

-
- Lavrac, V. (1999, January). *EXCHANGE RATE OF THE SLOVENIAN TOLAR IN THE CONTEXT OF SLOVENIA'S INCLUSION IN THE EU AND IN THE EMU*. Retrieved 09 07, 2011, from Inštitut za ekonomska raziskovanja: <http://www.ier.si/files/Working%20paper-01.pdf>
- Lavrac, V. (2004). *Fulfillment of Maastricht Convergence Criteria and the Acceding Countries*. Brussels: European Commission.
- Lavrac, V., & Majcen, B. (2006). *Economic Issues of Slovenia's Accession to the EU*. Ljubljana: Institute for Economic Research.
- Lesay, I. (2006). *Pension reform in Slovakia: the context of economic globalisation*. Brussels: European Trade Union Institute for Research, Education and Health and Safety (ETUI-REHS).
- Lopez, L. (2011, July 5). The Political Dynasties That Destroyed Greece, And The Real Reason The Country Is Such A Mess. *Business Insider*.
- Majcen, B., & et al. (2009). The Income Tax Reform in Slovenia: Should the Flat Tax Have Prevailed? *Eastern European Economics*, 5-24.
- Majcen, B., Verbic, M., Bayar, A., & Cok, M. (2009). The Income Tax Reform in Slovenia: Should the Flat Tax Have Prevailed? *Eastern European Economics*, 5-24.
- Malone, A. (2011, June 24). The Big Fat Greek Gravy Train: A special investigation into the EU-funded culture of greed, tax evasion and scandalous waste. *The Daily Mail*.
- Manolopoulos, J. (2011). *Greece's 'Odious' Debt*. New York: Anthem Press.
-

-
- Martínez-Vázquez, J., & Sanz-Sanz, J. F. (2007). Introduction. In J. Martínez-Vázquez, & J. F. Sanz-Sanz, *Fiscal Reform in Spain* (pp. 1-8). Northampton: Edward Elgar.
- Matsaganis, M. (2008). Progressive Modernization Defeated: Failing to Reform Pensions (1996–2002). In M. d. Carlo, *Challenge of Social Policy Reform in the 21st Century* (pp. 205-228). Athens: Sideris.
- Mitsopoulos, M., & Pelagidis, T. (2011). *Understanding the Crisis in Greece*. New York: Palgrave Macmillan.
- Mulas-Granados, C. (2006). *Economics, Politics and Budgets: The political Economy of Fiscal Consolidations in Europe*. New York: Palgrave Macmillan.
- Mundell, R: (1961). A Theory of Optimum Currency Areas. *Slovenia needs urgent reforms to skip recession: government institute*, 657-665.
- Navarro, V. (1997). The Decline of Spanish Social Democracy 1982-1996. *The Social Register*, 197-222.
- Novak, M. (2012, April 20). Slovenia needs urgent reforms to skip recession: government institute. *Chicago Tribune*, p. 1.
- OECD. (2005). *Greece*. Paris: Organization for Economic Co-operation and Development.
- OECD. (2009). *Revenue Statistics 2009*. Paris: Organization for Economic Cooperation and Development.

-
- Ofakoglou, I. (2012, 03 22). *Greek NHS: the battle continues to rage*. Retrieved 03 28, 2012, from PharmaPhorum: <http://www.pharmaphorum.com/2012/03/22/greek-nhs-battle-continues-to-rage/>
- Olsen, M. (2012). *Comparing German and Spanish Labour Markets*. Navarra: IESE.
- Ottawa, B. (2007). *Slovenia hears IMF age warning but cannot act*. London: Investment and Pensions Europe.
- Pagoulatos, G. (2002). *Greece, the European Union, and the 2003 Presidency*. Brussels: Notre Europe.
- Pampillón, R. (2008, 06 27). *Economía española*. Retrieved 04 7, 2010, from Instituto Empresa: http://economy.blogs.ie.edu/archives/2008/06/la_inflacion_po.php
- Pappas, T. (2010). *The causes of the Greek crisis are in Greek politics*. Florence: Open Economy.
- Pepelasis, A. (1990). Trends and Prospects of the Greek Economy. *European Affairs*, 85-89.
- Perez, S. A. (2004). Monetary Integration and a social model in Spain. In *Euros and Europeans: Monetary integration and the European Model of Society*. Cambridge: Cambridge University Press.
- Perez, S. A. (2004). Monetary Integration and a social model in Spain. In *Euros and Europeans: Monetary integration and the European Model of Society*. Cambridge: Cambridge University Press.
- Pezdir, R. (2006). Thirteen Years of Gradualism — Inhibiting Transition in Slovenia. *Post-Communist Economies*, 51-68.
-

-
- Pop, V. (2009, November 17). *Greece scores worst in corruption ranking*. Retrieved 11 24, 2011, from EU Observer: <http://euobserver.com/22/29003>
- Pridham, G. (2002). The European Union's Democratic Conditionality and Domestic Politics in Slovakia: The Mečiar and Dzurinda. *Europe-Asia Studies*, 203-227.
- Pridham, G. (2008). Status Quo Bias or Institutionalisation for Reversibility?: The EU's Political Conditionality, Post-Accession Tendencies and Democratic Consolidation in Slovakia. *EUROPE-ASIA STUDIES*, 423 – 454.
- Prunk, J. (2005). *The Creation of the Republic of Slovenia and its Development*. Retrieved February 8, 2012, from 15 Years of Slovenian State: <http://www.15years.gov.si/15-years/creation-of-slovenia/>
- PSOE. (2006). *Historia del PSOE: El primer gobierno socialista (1982-1996)*. Retrieved December 10, 2011, from PSOE: <http://www.psoe.es/ambito/historiapsoe/docs/index.do?action=View&id=997>
- Repe, B. (2010). *1989*. Retrieved February 7, 2012, from 20 Years of Independence: Republic of Slovenia: <http://www.twenty.si/first-20-years/89/>
- Reuters. (2011, January 25). Greece introduces lower uniform corporate tax rate. *Reuters*.
- Roccas, M., & Padoa-Schioppa, T. (2001). Economic Change and the Process of Democratization in Southern Europe. In D. Gibson, *Economic Transformation, Democratization and Integration into the European Union*. New York: Palgrave.
-

-
- Rodríguez López, A. (2005). Nueva Evidencia Empírica Sobre las Turbulencias Cambiarias de la Peseta Española, 1989-1998. *Estudios de Economía Aplicada*, 207-230.
- Sabic, Z., & Brglez, M. (2002). The national identity of post-communist small states in the process of accession to the European Union: the case of Slovenia. *Communist and Post-Communist Studies*, 67-84.
- Sadeh, T. (2006). *Sustaining European Monetary Union: Confronting the Cost of Diversity*. London: Lynne Rienner Publishers.
- Sala, V. D. (2004). EMU and the Italian Social State. In *Euros and Europeans: Monetary Integration and the European Model of Society*. Cambridge: Cambridge University Press.
- Schimmelfenning, Frank; Engert, Stefan; Knobel, Heiko;. (2006). *International Socialization in Europe*. New York: Palgrave Macmillan.
- Schularick, M. (2006). A Tale of Two 'Globalizations': Capital Flows from Rich to Poor in Two Eras of Global Finance. *International Journal of Finance and Economics*, 339-354.
- Šikulová, I. (2007). *Maastricht Inflation Criterion and Price Level Convergence in the New Member States*. Bratislava: Slovak Academy of Sciences, Institute of Economic Research.
- Silvia, S. J. (2004). Is the Euro Working? The Euro and European Labour Market. *International Public Policy*, 147-168.
- Sissouras, A., & Amitsis, G. (1994). Social security policy. In P. Kazakos, & P. Ioakimidis, *Greece and EC Membership Evaluated* (pp. 248-260). New York: St. Martin's Press.
-

Skledar, S. (2006). *Law on Collective Agreements (LCA)*. Institute of Macroeconomic Analysis and Development (IMAD).

Skledar, Š. (2007). *Trade unions oppose major reform of pension system*. Ljubljana: EIRO.

Skouras, T. (2001). The Greek Experiment with the Third Way. In P. Arestis, & M. C. Sawyer, *The Economics Of The Third Way: Experiences From Around The World* (pp. 170-183). Northampton: Edward Elgar Publishing.

Slovenska Tiskovna Agencija. (2011, June 11). 20 Years of Independent Slovenia. *Slovenska Tiskovna Agencija*.

Šmídková et al. . (2003). *Estimates of Fundamental Real Exchange Rates for the Five EU PreAccession Countries*. Prague: Czech National Bank.

Smith, W. R. (1998). *The left's dirty job: the politics of industrial restructuring in France and Spain*. Toronto: University of Toronto Press.

Sourbes, C. (2011, August 1). Spain not out of 'danger zone', must tackle deeper pensions reform – IMF. *IPE*.

Tamames, R. (1986). *Guía del Mercado Común Europeo: España en la Europa de los doce*. Madrid: Alianza Editorial.

TaxExperts Guide. (2012, January 01). *The Greek Tax Guide*. Retrieved March 28, 2012, from TaxExperts Guide: http://www.taxexperts.eu/en/GUIDE/TaxExperts_Guide

The Economist. (1999, December 09). Mikulas Dzurinda, Slovakia's turn for the better. *The Economist*.

The Economist. (2003, November 6). Fragile Reformer: A model of a modern prime minister. *The Economist*.

The Economist. (2005, April 14). The case for flat taxes. *The Economist*.

The Economist. (2006, June 19). The populist choice. *The Economist*.

The Economist. (2007, January 18). Flat taxes. *The Economist*.

The Economist. (2010, June 17). Fresh Air. *The Economist*.

The Economist Intelligence Unit. (2007, February). Country Report Slovakia. *THE Economist Intelligence Unit*, pp. 8-10.

Tompson, W., & Price, R. (2009). *The Political Economy of Reform: Lessons from pensions, product markets and labour markets in ten OECD countries*. OECD: Paris.

Townsend, M. (2007). *The Euro & Economic and Monetary Union*. London: John Harper Publishing.

Transparency International Greece. (2010). *GREECE: National In-depth Assessment*.

Triantafyllou, P. (2008). Pension Reforms in Greece: the Preferences of the Political Actor. In M. d. Carlo, *The Challenge of Social Policy Reform in the 21st Century* (pp. 229-262). Athens: Sideris.

Tsarouhas, D. (2012). Political Discourse and Path Shaping in Public Policy: Comparing Pension Reforms in Greece and Italy. *Public Administration*, March.

Turner, M. (2011, October 28). Ten things to know about the revamped EFSF. *Financial News*.

Vega Garcia, R., & Perez, C. (2000). Radical Unionism and the Workers' Struggle in Spain. *Latin American Perspectives*, 111-113.

Walsh, J. I. (2000). *European Monetary Integration & Domestic Politics*. London: Lynne Rienner Publishers.

Weyerstrass, K., & Neck, R. (2007, October 10). A New EU Member Country on the Road to the Euro Area: Monetary and Fiscal Policies for Slovenia. *International Atlantic Economic Society*, 431-449.

Wienberg, C. (2011, May 27). Greece 'Cheated' to Join Euro; Sanctions Since Were Too Soft, Issing Says. *Bloomberg*.

Willis, A. (2009, 10 22). Eurostat experience highlights doubts over Greek data. 1. Brussels, Belgium.

World Bank. (2010). *Ease if Doing Business*. Washington: World Bank.

World Bank and USAID. (2000). *Corruption in Slovakia: Results of Diagnostic Surveys*. Bratislava: World Bank and USAID.

WSJ. (2012, February 13). Europe's Debt Crisis. *The Wall Street Journal*.