

The future of the welfare state: paths of social policy innovation between constraints and opportunities

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Preconditions for Pacts on Income Policy: Bringing Structures back in. A comparison of Western Europe, 1980-2003

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Introduction

As an interaction of organized interests with public policy, 'social pacts' have attracted growing attention (e.g. Fajertag and Pochet, 1997; 2000). This can be traced to the counter-intuitive fact that the cooperation of organized business and labour and their involvement in public policy have been reinforced even though their long-term prospects have become less benign for such reasons as the rise of neo-liberalism and the decline in membership strength. Reflections on organized interests in general and pacts in particular require clarifying their relationship to earlier corporatist thinking. In this literature pacts find their counterpart in the concept of concertation, in particular as far as it refers to 'package deals' of organized business and labour with government, which are designed to tie pay policy to other policy fields (Lehmbruch, 1984). This raises the question of whether tripartite pacts mean continuation of corporatism. There are three answers to this question. First, pacts are indeed corporatist replicas, and their emergence is taken as evidence of the cyclical nature of corporatism (Schmitter and Grote, 1997). Second, pacts are an element of renewed (i.e. 'lean') corporatism that qualitatively differs from earlier, 'classical' corporatism in both functional as well as structural respects (Traxler, 2004). Third, pacts are structurally underdetermined. They are essentially contingent on such processes as exchange of information, strategies, dialogue and debate (e.g. Baccaro, 2003; Culpepper, 2002; Hassel, 2003).

Hence, the controversy centres on whether and how structures relate to pacts and other concertation policies. Whilst advanced corporatist theory makes the explicit distinction between structures of interest intermediation and practices of policy concertation (Schmitter, 1982), conventional corporatist reasoning assumes a tight nexus between them (e.g. Headey, 1970). Accordingly, corporatist arrangements are linked to encompassing, centralized and state-licensed structures of interest intermediation which equip organized interests with the ability to perform public policy functions. This assumption has been criticized for failing to explain the spread of pacts in a notable number of countries (e.g. Ireland, Italy, Portugal and Spain) where corporatist interest intermediation is absent.

The implications of this observation for the interplay of structures and policy are not evident. The process dimension is relevant since negotiations are inherent in pacts. However, the proposition that any interaction is embedded in a certain structural context belongs to the basics of social science. The structural context works as an incentive structure that defines the range of feasible options for action. This suggests a systematic relationship between action and structure. The fact that conventional corporatist reasoning cannot explain pacts does not imply dismissing the structure of interest intermediation as a key explanatory factor.

This study makes an analytical and empirical contribution to this issue. Its focus is on macro-level tripartite pacts on income policy for methodological, empirical and analytical reasons. Methodologically, this focus facilitates a clear-cut distinction of pacts from other concertation: It is difficult to demarcate mere consultation from pacting in policy fields other than income policy. Moreover, the preconditions for pacts on income policy may more or less differ from pacts on other issues (e.g. social welfare reforms), since the role of organized interests in pay fixing fundamentally differs from their role in public policies that fall within the purview of state responsibilities. Empirically, income policy is essential to most pacts (Hassel, 2000; Marginson and Sisson, 2004). Analytically, income policy represents the most genuine input which organized interests can make into public policy. This is because pay fixing remains within the purview of the two sides of industry, given free collective bargaining. Hence, income policy aimed at deliberately synchronizing pay movements with macroeconomic goals cannot work without voluntary cooperation of organized business and labour. Incomes policy was a key ingredient of Keynesianism, since demand management, as it was characteristic of the 1960s and 1970s, required being flanked by incomes policy as a means of keeping active fiscal policy compatible with low inflation. After the shift to orthodox, supply-side economics that occurred in the early 1980s, deregulation and monetarism have increasingly exposed wage formation to the disciplining forces of the market, such that income policy should have become pointless. In contrast to this, numerous pacts on income policy were struck in several countries from the early 1980s onwards. This paradoxical coincidence brings preconditions for pacts on income policy to the forefront of research on organized interests and public policy: The survival of an allegedly outdated mode of concertation puzzles research even more than the rise of

pacts on issues that relate to new governance demands.

The next section argues that the general assumption of utmost importance of interest intermediation still holds. What is wrong is the way in which it was elaborated by corporatist theory. The essence of our argument is that multi-employer bargaining whose pay policy is not dominated by the exposed sector provokes pacts on income policy, in stark contrast to alternative bargaining structures. The paper then proceeds to present hypotheses on the determinants of the conclusion of pacts and their stability. The following section contains the empirical analysis. After specification of the measures and the statistical models the hypotheses are tested on time-series data for 14 western European countries in the period from 1980 to 2003. The concluding section discusses the theoretical and political implications of the empirical findings.

Corporatism, the bargaining structure and pacts

Conventional corporatist thinking assumes a certain match of structure and policy in that centralized interest intermediation, namely bargaining centralization, is the key prerequisite for macro concertation. This thesis rests on two false propositions on the interaction between interest intermediation and macroeconomic performance.

The first one posits that a country's macroeconomic performance monotonically increases with the degree of centralization of collective bargaining because growing centralization hinders the bargainers from externalizing the costs of their pay increases (e.g. inflation, unemployment) on to the public (e.g. Cameron, 1984). Calmfors and Driffill (1988) have amended this proposition. Assuming perfect competition, their hump shape thesis contends that extremes (i.e. highly centralized and highly decentralized bargaining) perform well, while the performance of intermediate centralization (i.e. industry-level and occupational bargaining) is poor. The good performance of decentralized (i.e. single-employer) bargaining is traced to (perfect) competition in product markets which preclude the companies from passing their pay hikes on to their product prices. In contrast to this, intermediate bargaining is argued to be able to externalize its pay increases, since it works like a cartel. There are

several problems with this thesis. Real markets are not subject to perfect competition. The thesis downplays market internationalization. Since the scope of industry-level bargaining is always limited to a certain territory, its ability to cartelize markets decreases with growing exposure of an industry to international competition. The thesis also ignores that coordination of industry-level bargaining across the economy can work as a functional equivalent to centralized bargaining (Soskice, 1990). More recent research has emphasized that the performance of both centralization and coordination is highly contingent on circumstances (e.g. Franzese, 2002; Garrett and Way, 1999; Traxler, 2003). Its essence is that centralization is not necessarily the best way to superior performance.

The second problem with corporatist orthodoxy is that it implies a natural selection of institutions. There is tendency to deduce trends towards centralized interest intermediation from concertation requirements (e.g. Lehmbruch, 1982). However, a need does not generate its own fulfilment. Actors may find themselves trapped in poorly performing institutions if costs of change outweigh its benefits (North, 1990).

The upshot of these considerations is that there are notable degrees of freedom in how the bargaining structure and policy relate to each other. Yet, these degrees of freedom are not unlimited. As regards income policy, they are restrained by the need for pacts and their feasibility which are both determined by the bargaining structure and its broader context.

The determinants of pacts

When dealing with the emergence of pacts, one may differentiate between three aspects: the willingness of the actors to conclude a pact; the conclusion of a pact; and its stability. Although they are not reducible to each other, the literature on pacts has shown a tendency to conflate them (Baccaro and Simoni, 2006). Addressing the first aspect creates severe methodological problems especially for a comparative quantitative study: Finding reliable data is harder for the actors' willingness than for the conclusion and stability of pacts. If we have evidence that an actor expressed its willingness to engage in pacts, the question remains whether this initiative is true or merely tactical. The fact that the distinct

actors may differ in their willingness also adds to the conceptual problems with explaining this phenomenon. We thus confine our analysis to the two other aspects. Their determinants may somewhat differ, leading to manifold configurations of the incidence and viability of pacts. For instance, there may be a proliferation of short-lived pacts or a few, long-lived pacts.

To specify the determinants of pacts, we follow the point that action is embedded in a certain context. Unpacking its components, we address (i) the *economic policy regime*, (ii) the *bargaining structure*, (iii) *political conditions*, (iv) the *properties of the associations and their role in public policy* and (v) the *economic situation*.

(i) As regards the *economic policy regime*, the question is why income policy has not withered away after the shift to orthodox economics, but has been revived by pacts. As this shift has been designed to replace non-market institutions with market competition, the revival of income policy indicates that this replacement has remained incomplete. One unintended effect of neo-liberal measures to deregulate markets has been a deepening of differences in exposure to market competition. In this respect, the divide between the trading sectors such as manufacturing, which are strongly exposed to international competition, and the non-trading sectors, namely the public sector, which are still sheltered from international competition, is most accentuated.¹ This sectoral divide translates into differences in leeway for pay demands. When being sheltered from international competition, sectors can still externalize the costs of their pay increases. If they do so by enforcing pay hikes that exceed their (rather low) productivity growth, they produce negative externalities for the exposed sectors: Inflationary pay policies in the sheltered sectors impair the international competitiveness of the exposed sectors in manifold ways: higher input prices, shortages of qualified labour, and a higher tax burden. Monetary conservatism as a key component of orthodox economics exacerbates rather than eases these problems. If monetary policy is tightened in response to inflationary pay policies of the sheltered sectors, this primarily harms the exposed sector through higher interest rates and real exchange rate appreciations. Hence, there is an asymmetrical interdependence of the exposed and sheltered sectors in terms of pay policy. Even when the exposed sectors embark on wage moderation, this does not suffice to improve or sustain their international competitiveness. What is needed in addition is pay restraint in the sheltered sectors. This asymmetrical

interdependence essentially characterizes orthodox economics and its emphasis on a credibly conservative monetary regime.² Under Keynesianism, with its accommodating monetary policy, the threat to international competitiveness, as caused by pay movements in the sheltered sectors, could be cushioned through exchange rate devaluations.

(ii) While orthodox economics thus give rise to these sectoral asymmetries, the national *bargaining structures* in Western Europe tend to reinforce them institutionally. With the exception of the UK, industry-level pay bargaining is generally important, and even predominant in most countries (Traxler et al., 2001). Reflecting asymmetrical exposure to world market competition, industry-level bargaining tends to generate contrasting effects in the sheltered and the exposed sectors. Industry-level bargaining for the sheltered sectors is most capable of externalizing the negative effects of its pay hikes, in line with what Calmfors and Driffill (1988) predict for intermediate bargaining in general. In contrast to this, international competition compels industry-level bargaining for the exposed sectors to moderate their pay policies (Crouch, 1993).

Given asymmetrical world market exposure and industry-level bargaining under an orthodox economic policy regime, the key problem of aligning pay policy with macroeconomic requirements is pay moderation of the sheltered sectors. Following the above review of the literature on the performance of bargaining structure, one can differentiate the following strategies to cope with this problem: complete bargaining centralization; complete decentralization; and economy-wide coordination which is performed either by the central-level peak associations of business and labour or by pattern-setting of the bargaining units of the exposed sectors.

In practice, there is no difference between centralized bargaining and peak-level coordination since central-level settlements are non-binding guidelines. Centralized bargaining is part of a more or less articulated multi-level system which usually includes industry-level bargaining. For reasons of conceptual parsimony, we differentiate only between decentralization, peak-level coordination in the broad sense (i.e. including centralized bargaining), and coordination by pattern bargaining of the exposed sectors. Aside from the UK, where full-fledged decentralization has made coordination activities across the economy unfeasible, all other countries under consideration have embarked on coordination efforts, with pattern bargaining covering the minority of countries: Austria, Germany,

and, from the late 1990s onwards Sweden. There are so few cases of exposed-sector pattern bargaining because it presupposes a specific power configuration, enabling the exposed sectors to set the pace for overall pay movements.

Decentralization of bargaining to the single-employer level is at odds not only with bargaining coordination, but also with pacts on income policy because the bargaining units are so small that they lack encompassing grip on pay movements. In countries where single-employer bargaining prevails it covers one third of all employees at best (Traxler et al., 2001). Another problem is that it embraces a multiplicity of small bargaining units whose pay policies can hardly be coordinated. Hence, decentralized bargaining structurally precludes pacts on income policy, even if there is a need for them.

The distinction between complete decentralization and coordinated bargaining marks the divide between unfeasibility and feasibility of pacts. Therefore, we can concentrate on the two forms of bargaining coordination when it comes to analyzing the need for pacts. Comparative analysis suggests that exposed-sector pattern bargaining delivers effective pay moderation more consistently than peak-level coordination (Traxler et al., 2001). This is because pattern bargaining rests on a market-driven coordination agenda, whereas peak-level coordination is far more politicized: When compromising on aggregate pay hikes, it must simultaneously deal with (re)distributional issues of inter-sectoral pay differentials. To maximize legitimacy, the coordination goal of the peak organizations is skewed to the 'median affiliate' whose interests are likely to differ from the exposed sectors, as the union peaks organize strong public-sector affiliates. Vertical coordination problems add to these horizontal ones. Peak-level coordination faces more problems than pattern bargaining, when it comes to making the shop floor comply with its coordination goals. Hence, peak-level coordination tends to produce worse performance effects than any other bargaining structure, if either the public sector dominates the coordination process (Franzese ,2002; Garrett and Way, 1999) or effective means of binding the shop floor are lacking (Traxler et al., 2001; Traxler, 2003). This volatility of effectiveness is accompanied by instability of the structure per se, leading to occasional collapse of the coordination process even in strongly corporatist countries such as Finland and Norway.

With the exception of exposed-sector pattern bargaining, any form of multi-employer

bargaining (i.e. industry-level bargaining, central-level bargaining, or a combination of them), which covers the sheltered sectors, is beset with considerable problems of synchronizing their pay policy with macroeconomic requirements. These problems with industry-level bargaining and related peak-level coordination provoke state interference, aimed at stabilizing the cooperation of the two sides of industry and improving their performance. There are two options for the state: suspending free collective bargaining by imposing statutory pay controls, or initiating tripartite pacts on income policy. State-imposed pay coordination is certainly the second best choice, as it magnifies the legitimation problems the authorities have to face.

(iii) Regardless of this, there is no clear road to tripartism. It has been argued that its prospects are contingent on *political conditions* insofar as concertation combines with labour governments rather than alternative government arrangements (e.g. Lange and Garrett, 1985). This thesis holds for the 1970s rather than for the following decades (Traxler et al., 2001). The close association between labour governments and tripartite income policy was bound to Keynesianism. Given active fiscal policy and full employment, the unions had an alternative to cooperation all the more since widespread shop floor militancy during the late 1960s and early 1970s encouraged them to pursue redistributive pay policies. In these circumstances, their special relationships with the union movements made labour governments better prepared for building tripartism. This has changed under orthodox economics. Rising unemployment and monetary conservatism have weakened the labour market power of the unions so much that tripartism is welcomed as a political source of power. Therefore, labour governments have lost their special appeal to union cooperation. While they could offer more generous compensation for wage moderation under Keynesianism, non-labour governments may now have even the better bargaining chips because they can pose more credible threats to the unions in case of non-cooperation. In the new context of open economies with (quasi)fixed exchange rates any government is interested in tripartite income policy since the new key issue of income policy, international competitiveness, concerns conservative parties no less than social democracy (Crouch, 2000). Another political factor which is highlighted in the literature is government strength insofar as weak governments need pacts as a source of exogenous support for their policies (Avdagic, 2008; Baccaro and Lim, 2007; Hamann and Kelly, 2007). However, the

impact of government strength may be conditional on the subject of pacts. Weak governments seek support from pacting in matters they are fully responsible for. Conversely, strong governments are more able to prompt business and labour to subscribe to income policy, if free collective bargaining fails to moderate pay. Since many pacts combine income policy with other issues, the net effect of government strength may be statistically insignificant.

(iv) How do pacts on income policy relate to corporatism? As outlined above, the propensity to conclude pacts does not monotonically increase with bargaining centralization but is present at any bargaining level other than single-employer bargaining, unless exposed-sector pattern bargaining is established. Aside from bargaining centralization, *union strength*, *associational concentration* and *associational participation* in public policy are properties of corporatism which may affect the prospects for pacts. The standard argument is that corporatism requires powerful unions (Korpi, 1978). Again, this proposition fits Keynesianism more than its successor. Under Keynesianism union strength was an important precondition for controlling the shop floor in line with the goals of income policy. Moreover, the emphasis on union strength is biased towards Scandinavian experiences and ignores corporatist arrangements in other countries, where the employer side is stronger than the unions (Crouch, 1993). Under orthodox economics the relationship between strong unions and income policy may have disappeared or changed. Very weak unions can hardly be a reliable partner of governments, whereas strong unions may reject pacts, since supply-side policies can offer them little compensation for wage moderation. This suggests a hump-shape relationship between union strength and pacts (Ebbinghaus and Hassel, 2000). Associational concentration increases with the number of actors decreasing. It is presumed to be essential to corporatism because associational concentration makes actors encompassing, enabling them to internalize negative externalities. We argue that this factor is dominated by the bargaining structure. Regardless of the degree of concentration, governments are likely to intervene in bargaining, if problems with pay moderation are endemic. Nevertheless, a high degree of concentration may stabilize pacts, because the scale of coordination problems declines with growing concentration. We assume an analogous relationship between associational participation and pacts. Governments will launch pacts on income policy if the bargaining structure generates a corresponding need. Associational participation in public policy fields other than income policy may

help consolidate pacts because concerted policy fields enlarge the zones of compromising.

(v) The *economic situation* is assumed to matter in two respects (e.g. Hancké and Rhodes, 2005). Pacts are struck in response to serious country-specific problems of economic performance, and they are a reaction to transnational (i.e. symmetrical) adjustment shocks. During the period under consideration such shocks are generated by the establishment of the Single European Market and European Monetary Union.

The above considerations enable us to deduce testable hypotheses. The key explanatory factor is the bargaining structure. In line with our argument, the relevant differences in the bargaining structure are categorical: We have to differentiate between four bargaining categories: Single-employer bargaining, exposed-sector pattern bargaining, ‘unpatterned’ multi-employer bargaining, and state-imposed pay coordination. These categories condition pacts as follows:

- Single-employer bargaining, when prevailing throughout the economy, is at loggerheads with pacts. This is mainly because this bargaining category does not provide such grip on pay movements that incomes policy requires.
- Exposed-sector pattern bargaining does not stimulate pacts, because it works as a substitute for income policy. If the exposed sectors set the pace for pay setting in the sheltered sector, then the pay rises are moderated on aggregate, such that they are in line with the imperatives of international competitiveness. Therefore, there is no reason for governments to step in.
- State-imposed pay control is also a substitute for income policy. Governments may resort to them if any other kind of pay moderation is ineffective.
- ‘Unpatterned’ multi-employer bargaining is the only bargaining category which induces pacts. In this case strong intermediate bargaining units lack economy-wide coordination by the exposed sectors. There are two variants of strong intermediate bargaining units: Intermediate bargaining is important in all sectors. Alternatively, intermediate bargaining is important in the sheltered sectors, whereas bargaining is more decentralized or centralized in the exposed sectors. Both variants empower the sheltered sectors to externalize their pay rises. The public sector nowadays forms the backbone of the sheltered segment. It is not only cartelization but also political weight which empowers intermediate bargaining for the public sector to

externalize its pay policy. Neoliberal attempts at fiscal discipline are no functional equivalents to world market competition. Cash limits are not very credible: Governments are likely to refrain from cutting back services and employment which large sector-wide pay rises, as fixed by multi-employer bargaining, would imply, because such measures threaten to undermine their legitimacy (Calmfors, 1993). 'Unpatterned' multi-employer bargaining thus provokes governments to launch pacts even when the peak organizations of business and labour for their own part try to orchestrate the pay policies across all sectors, since such bipartite peak-level coordination is notoriously unstable and also uncertain with regard to its outcomes.

This key hypothesis is complemented by seven hypotheses on the other contextual components:

- Government partisanship does not systematically affect pacts.
- Government strength interacts with the issues covered by pacts. On aggregate, its effect is insignificant.
- Associational concentration does not influence the conclusion of pacts, while existing pacts become more sustainable with growing concentration.
- Associational participation in policy areas other than income policy works in a way analogous to concentration.
- The relationship between union strength and pacts is either hump-shape or monotonically positive.
- If a country faces extraordinary economic problems, then this increases the likelihood of pacts.
- The need to prepare for the single market and EMU strengthened the trend towards pacts.

Measures, model specifications and empirical findings

Details of measures and data sources are summarized in the appendix. We explain here their conceptual background. Part of the literature conceives macro-level accords that involve only the peak organizations of business and labour also as pacts. In contrast to this, we consider here only pacts which are tripartite in the sense that governments have an active role in their conclusion. What matters

is actual rather than formal state involvement: Tripartism is given if either governments are formally party to an accord, or informally operate as catalysts, setting incentives for business and labour to reach an agreement. There are two reasons for this focus on tripartism. First, understanding purely bipartite accords of business and labour as pacts blurs the analytical distinction between free collective bargaining and public policy. If the concept of income policy makes sense, then it is state involvement as its constituent property. Bipartite macro accords are simply a case of centralized bargaining. Second, including centralized bargaining into the category of pacts on income policy ends in tautology in our case, because this means that centralized bargaining becomes part of the dependent variable as well as of an independent variable. Our study captures pacts on income policy of macro (i.e. cross-sectoral) scope. They explicitly aim to govern pay movements, committing the two sides of industry to pay moderation for the sake of macroeconomic goals. According to this definition pacts may either cover only pay moderation or extend to other policy areas, and they may issue concrete figures or basic principles for lower-level bargaining.

The stability of pacts is measured as duration. If their duration is unspecified, it is estimated on the basis of information provided by country experts. Unlike other studies, we do not differentiate between ‘successful’ and ‘unsuccessful’ pacts. Methodologically, this again avoids arbitrary classifications.

These definitional criteria clearly demarcate pacts on income policy from other pacts struck in the 14 countries over the relevant period, with the notable exception of the German Alliance for Jobs. The Alliance was not designed to introduce income policy, as none of the numerous working groups and topic-related dialogues dealt with this issue (Bispinck and Schulten, 2000). In practice, it was burdened with severe controversies over whether issues of collective bargaining should be addressed. In 2000 the Alliance nevertheless issued one statement on pay setting. However, it remained rather vague, when relating well-established bargaining principles to the need to create jobs. This makes the statement a borderline case. Balancing all aspects, however, suggests that taking the statement as a case of income policy rather overstretches the concept.

Measuring the bargaining structure (BS) results in unequivocal country classifications except for four countries. The Belgian laws of 1986 and 1996 require the peaks of business and labour to

align their pay hikes with those in the main trading partners, and authorize the government to establish pay controls if voluntary pay restraint fails. Pacts are coded for the years which were covered by a peak-level agreement, and state-imposed pay coordination is coded otherwise. The French bargaining structure is classified as a case of state-imposed pay coordination since most industry-level settlements ratify the statutory minimum wage. In Ireland single-employer bargaining dominates on aggregate, while intermediate bargaining is important in the sheltered sectors. Public-sector bargaining is strongly centralized. This exceptional configuration makes Ireland's bargaining system especially prone to pay policies externalizing public-sector settlements on to the exposed sectors, unless income policy dams these tendencies. Hence, Ireland is classified as 'unpatterned' multi-employer bargaining.

Thoroughgoing decentralization has made single-employer bargaining prevalent throughout the UK economy. In the public sector the state also tightened its rein by establishing Pay Review Bodies which rescinded the bargaining right of major groups of employees. Since the shift to single employer bargaining was a continuous process, it is difficult to assess when it became definitely prevalent. It was already in the late 1960s when informal workplace bargaining hollowed out the formal system of multi-employer bargaining. From the outset the Thatcher government confronted the public-sector unions, along with measure to undermine the sector's national bargaining structures. It is thus reasonable to subsume the UK under single-employer bargaining for all years under consideration, although the early 1980s are borderline cases.

Table 1 documents the data on pacts and the bargaining structure. Two borderline cases remain (i.e. Germany and the UK) which are registered by putting the alternative scores in brackets.

- Table 1 about here -

As far as the other measures are concerned, government partisanship refers to leftist parties (LEFTGOV) because classic corporatist theory assigns a key role to them in initiating income policy. Cabinet changes during a year are weighted averages, unless a pact is concluded in that year. In this case the score refers to the leftist party cabinet portfolio which applied to the date at which the pact was concluded.³ Government strength (GS) means parties seats as a percentage of all seats in lower house. Changes in GS are captured in the same way as cabinet changes. The measure of associational concentration is the number of peak union organizations (NPU). Peak union organizations are cross-

sectoral associations which are specialized in coordinating their lower-level members. Associational participation is measured as involvement of the largest union peak organization in public policy other than income policy (UPP). We refer to the unions because they have the critical role in income policy, as they are required to moderate their demands. Moreover, union systems are significantly more fragmented than association of employers (Traxler et al., 2001), with the consequence that that the union systems create more coordination problems. Union participation in public policy significantly correlates with business participation (Traxler et al., 2001), such that involvement of the unions indicates the degree of associational participation in general. The measure of union strength is net union density (UD). To test the impact of union strength, we use UD and its square. The squared term relates to the hump-shape relationship. The economic situation is defined as the difference between unit labour cost growth during the focal sub-period (see below) and unit labour cost growth over the entire period under examination (RELULC). If pacts are concluded so as to cope with a situation of economic crisis, then RELULC is expected to exert a significantly positive effect on the incidence of pacts. We concentrate here on unit labour costs since they are more directly subject to income policy than other performance criteria. To capture the impact of the single European market and EMU, we proceed from the time period covered by the year when the Single European Act and the Maastricht Treaty were signed until the year when it went into effect. This period (SEAEMU) is understood as preparatory time which is hypothesized to stimulate pacts in those countries which participated in these integration projects.⁴ For the EFTA countries, this variable includes the European Economic Area Agreement.

Furthermore, we have to control for budgetary and monetary conservatism since orthodox economics expects this policy-line to work as a functional equivalent to tripartism. Our measures are budget deficit (BD) and central bank independence (CBI).

To test our hypotheses, we adopt a multivariate regression design that combines cross-sectional and longitudinal analysis.⁵ To take account of the difference between the conclusion of pacts and their stability, we specify two basic models, one based on periodized data, and the other, on annual data. The periodized data are aggregates for sub-periods (i.e. 1980--82, 1983--85, 1986--88, 1989--91, 1992--94, 1995--97, 1998--2000, and 2001--03).⁶ For the dependent variable, the

periodization implies that each period in the course of which at least one pact is *concluded* is coded as a sub-period of pacts. This measure (PACTS/C) is insensitive to the duration of pacts. Therefore the models for periodized data focus on the conclusion of pacts. The scores for the independent variables refer to the years in which the pact is concluded, with the exception of the economic situation (RELULC), budgetary deficits (BD) and union participation in public policy (UPP). Since pacts are hypothesized to be a response to economic problems, it is reasonable to lag RELULC and BD by one sub-period.⁷ Likewise, UPP must be lagged since it is regarded as a precondition for pacts. The models for annual data centre on the *stability* of pacts (PACTS/S), since they register any year from the conclusion of a pact until the end of its duration.

Set up as pooled time-series-cross-section OLS regression analysis with panel-corrected standard errors, two basic models are estimated, one for annual data and one for periodized data, with j , i , p and t standing for the bargaining categories, the countries, sub-periods and years covered, respectively, and ε denoting the error term. Since Durbin-Watson statistics indicate serial correlation in the case of Model (1), a first lag of the dependent variable is entered.

$$(1) \quad PACT_{it} = \beta_0 + \beta_1 UD_{it} + \beta_2 UD_{it}^2 + \beta_3 LEFTGOV_{it} + \beta_4 UPP_{it-1} + \beta_5 NPU_{it} + \beta_6 SEAEMU_{it} + \beta_7 CBI_{it} + \beta_8 GS_{it} + \beta_9 PACT_{it-1} + \sum \beta_j BS_{jit} + \varepsilon_{it}$$

$$(2) \quad PACT_{ip} = \beta_0 + \beta_1 UD_{ip} + \beta_2 UD_{ip}^2 + \beta_3 LEFTGOV_{ip} + \beta_4 UPP_{ip-1} + \beta_5 NPU_{ip} + \beta_6 SEAEMU_{ip} + \beta_7 CBI_{ip} + \beta_8 GS_{ip} + \beta_9 RELULC_{ip-1} + \beta_{10} BD_{ip-1} + \sum \beta_j BS_{jip} + \varepsilon_{ip}$$

Since the institutional predictors are rather ‘sticky’, and a full set of country dummies is not appropriate to the problem, we examine the robustness of these TSCS models by employing the fixed effects vector approach (Plümer and Troeger, 2007).⁸ Each of these two pairs of models is estimated for the standard coding and the alternative coding of the two borderline cases.⁹ Altogether, this yields 8 models.

Regressing the conclusion and stability of pacts on our eight predictors creates concern about endogeneity in two cases. Union participation (UPP) may stabilize pacts on income policy; conversely, pacts may also pave the way for involving organized interests in broader areas of public policy. The economic situation and pacts are also interdependent. Since pacts are devised to improve

performance, the economic situation when defined in terms of performance (i.e. RELULC and BD) becomes endogenous to pacts within the framework of a longitudinal design, unless pacts are notoriously ineffective. The endogeneity problems are less severe in the case of the periodized model because the lag per one sub-period captures a relatively long time. Compared to the economic situation, UPP is less likely to be endogenous, since it shows far less variations over time than the incidence of pacts. To detect endogeneity of UPP for both models, and endogeneity of RELULC and BD for the periodized model, Granger Causality Tests were employed. Since the results were insignificant in all cases, the endogeneity assumption could be rejected.

The results for the models are summarized in Table 2. They point to the same direction and enable us to discuss them altogether. The coefficients for the bargaining structure (BS) are average deviations from the reference category, i.e. 'unpatterned' multi-employer bargaining. Each of the three other bargaining categories significantly differs from the reference category in that they record a far lower incidence of pacts. Union participation (UPP) shows a significantly positive effect in Models 1c and 1d. It slightly fails the level of statistical significance in Models 1a and 1b, with $p = 0.08$ and 0.07 , respectively. In Models 2a--d, UPP remains generally insignificant. This indicates that UPP is conducive to the sustainability of pacts rather than to their conclusion, although the sustainability effect is not very robust. No other variable is significant in any Model. Overall, these findings lend strong empirical support to our hypothesis on the pre-eminent impact of the bargaining structure on the conclusion and stability of pacts, and they provide modest evidence for our hypothesis on the differential effect of associational participation on the conclusion and stability of pacts. The insignificance of leftist parties in government also confirms our expectations. None of the four other hypotheses is corroborated by the models.

- Table 2 about here -

Recalling conventional wisdom that considers pacts a response to outstanding economic problems (e.g. Hancké and Rhodes, 2005) it is amazing to find both labour cost growth (RELULC) and European economic integration (SEAEMU) insignificant. As alternatives to RELULC, we used other relative performance criteria such as inflation and unemployment. Running the regressions with these criteria did not change the results. The way in which RELULC captures a country's economic

situation follows an 'indigenous' logic insofar as its situation in a certain sub-period is measured relative to its average performance from 1980 to 2003. One may argue that pressures of international competitiveness prompt countries to interpret their situation in comparison with other countries. Several countries concluded pacts explicitly relating their labour costs to those of their main trading partners. Hence, we tested indicators of unit labour cost growth, inflation and unemployment that measure a country's performance in sub-period p compared to the average performance of 19 OECD countries over the same sub-period. Again, all these indicators proved insignificant. One explanation for this is that pacts are not always driven by poor performance. There is a tendency to give pacts a pro-active role aimed at preventing economic problems (Hassel, 2003).¹⁰ As serial correlation in Model 1 indicates, pacts have become reiterated practice in several countries, such that they are not bound to poor performance, but may be reproduced because of satisfactory outcomes (Avdagic et al., 2005). The general lesson is that the perception of economic problems as well as related measures is mediated by the properties of the respective country, namely its bargaining structure. This applies also to the response to European economic integration. If the bargaining structure inclines a country to respond by pacts, it will do so regardless of the kind of economic challenge. Conversely, bargaining structures that discourage countries from pacts have this effect also when it comes to adjusting to economic integration. Overall, the effect on pacts of the bargaining structure clearly prevails over situational factors such as economic problems, European market integration and government partisanship.

Conclusions

There is a close nexus between structures and agency, as far as income policy is concerned. However, this nexus does not fit orthodox corporatist theory which assumes strong association between bargaining centralization and concerted incomes policy. Centralization is not irrelevant, since the distinction between single-employer bargaining and multi-employer bargaining marks the threshold for the *feasibility* of income pacts. However, the *need* for them depends on how multi-employer

bargaining interacts with the asymmetrical interdependence of the exposed and sheltered sectors. Since exposed-sector pattern bargaining ensures pay moderation without state interference, such a need emerges only in the case of ‘unpatterned’ multi-employer bargaining which essentially includes the sheltered sectors. Depending on whether the German Alliance for Jobs is taken as a case of income policy, ‘unpatterned’ multi-employer bargaining is a *necessary* precondition for pacts or comes close to that. It is certainly not a *sufficient* precondition, as the bargaining structure changes little (Table 1). Hence, this variable explains differences in the occurrence of pacts across countries rather than differences within countries over time. Structures are thus significant primarily in cross-national perspective, whereas within-country variations mainly originate in processes with its various and manifold nuances that a quantitative comparison cannot capture.

Our findings also differ from corporatist orthodoxy in how the bargaining structure fosters pacts. The orthodox view is that bargaining centralization clusters with income policy, because centralization most effectively internalizes pay externalities. In contrast to this, our theoretical argument and the empirical results suggest that the best-performing bargaining category does *not* give rise to pacts: Exposed-sector pattern bargaining moderates pay movements so effectively that the state is not forced to intervene. Conversely, the performance of ‘unpatterned’ multi-employer bargaining, even when being coordinated by the peaks of business and labour, is so volatile that this prompts state-led attempts at income policy at least from time to time. Put otherwise, corporatist orthodoxy expects pacts to associate with centralized bargaining, because this is believed to work as a *problem-solving* vehicle for pay moderation. According to our analysis, however, ‘unpatterned’ multi-employer bargaining paves the way for pacts, because it is a *problem-generating* mechanism.¹¹ Whether state intervention by income policy actually solves the problem is contingent on circumstances. Hence, the uncertainties of performance that plague ‘unpatterned’ multi-employer bargaining continue in a context of income policy. Governments are likely to re-launch pacts even when previous efforts failed. This is because alternative modes of state interference in pay fixing are far less attractive than income policy: There is the politically risky option of statutory pay controls; and there is the thorny task of dismantling multi-employer bargaining.

It has been speculated that pacts on income policy are on the wane in Western Europe, since

the incentive to continue with them has disappeared after accession to EMU (Hancké and Rhodes, 2005). In contrast to this, our empirical findings suggest that the stimulating effect of EMU on pacts has widely been over-estimated. As the preparations for the single market and EMU did not significantly boost the spread of pacts, so accession to EMU will not crowd out them significantly. As we have seen, the driving force behind the tendency to conclude pacts is asymmetrical exposure of sectors to growing market internationalization in a context of ‘unpatterned’ multi-employer bargaining. This situation creates a need for concerted pay moderation which is not eased by accession to the eurozone. While there will always be fluctuations in the incidence of pacts, the appreciation of the Euro and expansionary macroeconomic policy in response to the current crisis will rather exacerbate this need in the mid-term. In the long run, pacts will (re)appear as long as ‘unpatterned’ multi-employer bargaining persists, along with sectoral asymmetries in world market exposure.

Endnotes

¹ Privatization as a supplement to deregulation does not overcome this asymmetry. Quasi-monopolistic situations often survive, giving the employees similar power as public employment (Crouch, 2000).

² EMU has not changed this. The ECB is committed to monetary conservatism, and EMU deprives its countries of national exchange rate policy as a means of adjusting to ‘excessive’ pay increases, as caused by the sheltered sectors.

³ Dates for cabinet changes are taken from www.marquette.edu/polisci/swank/htm.

⁴ Denmark is classified as being involved in the EMU preparations since it signed the Maastricht Treaty conditional on a referendum.

⁵ This approach is superior to such alternatives as QCA. Categorizing or ranking metric variables at often questionable cut-off points can be avoided. Only regression can capture the dynamic dimension of pacts.

⁶ These aggregates are means for the metric variables, and modal values for the categorical variables.

⁷ If more than one pact is concluded during a sub-period the aggregates for the independent variables other than the economic situation refer only to the years in which the pacts were signed.

⁸ We apply the three-stage fixed effects vector decomposition modelling approach, differentiating between time-invariant variables (UPP, NPU, BS), rarely changing variables (SEAEMU, CBI, GS) and as varying variables (other predictors).

⁹ Further robustness tests include inspection of multicollinearity and the use of several alternatives to RELULC (see below).

¹⁰ In comparison to Keynesian income policy, this tendency under orthodox economics results from the need to anticipate monetary policy which the parties to income policy do not control.

¹¹ Epistemologically, this difference means that we offer a causal explanation for pacts, whilst that of corporatist orthodoxy is teleological.

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Appendix:

Variable definitions and sources

BD	Budget deficit as total central government debt (% of GDP) (OECD <i>Economic Outlook</i>).
BS	Bargaining structure: BS1 = ‘unpatterned’ multi-employer bargaining; BS2 = uncoordinated single-employer bargaining; BS3 = exposed-sector pattern bargaining; BS4 = state-imposed income policy (Own data).
CBI	Central bank independence increases with score (Cukierman, 1992; Polillo and Guillén, 2005).
GS	Government strength as % of seats in lower house held by the government (http://www.wzb.eu/alt/ism/people/misc/cusack/d_sets.en.htm#data).
LEFTGOV	Leftist parties in government as a percentage of cabinet seats. We thank Manfred G. Schmidt (University of Heidelberg) for providing the data.
NPU	Number of national peak union organizations (Own data).
PACTS/C	Number of sub-periods (i.e. three-year intervals) during which pacts were concluded (Table 1).
PACTS/S	Years in which pacts were concluded or effective (Table 1).
RELULC	Relative unit labour costs: nominal growth over sub-period p minus growth over the entire period (OECD, <i>Economic Outlook</i>).
SEAEMU	Preparatory phase of Acts of European economic integration: Single European Act, Maastricht Treaty on EMU, and European Economic Area Agreement. Coded as 1 for countries involved. (Own data).
UD	Net union density (OECD for 1980--2003; own data for 2003).
UPP	Union participation in public policy: aggregate index of 11 activities: 1 = influencing government or parliamentary bodies with regard to labour market issues; 2 = representing members’ labour market interests on national corporatist institutions; 3 =

conducting consultations with business confederations; 4 = participating in formulation of industrial policy programs; 5 = participating in formulation of regional development programs; 6 = participating in formulation of occupational training programs and active labour market policy; 7 = participating in formulation of R&D programs; 8--11 = participating in the implementation of (4)--(7). Each activity counts as 1. (Own data).

Own data based on responses from country experts to a standardized questionnaire.

Tables

TABLE 1 Pacts on income policy and bargaining structure

Countries	Pacts		Bargaining structure (BS)
	Conclusion	Duration*	
Austria	No pacts		BS3: 1980--2003
Belgium	1998, 2000, 2003	1998--2003	BS1: 1980--81; 1986--93; 1998-- 2003 BS4: 1982--85; 1994--97
Denmark	1987, 1999	1987--97; 1999--2003	BS1: 1983--84; 1987--97; 1999-- 2003 BS3: 1981--82 BS4: 1980; 1985--86; 1998
Finland	1981, 1984, 1986, 1988, 1990/91, 1995, 1997, 2000, 2002	1981--87; 1989--93; 1995--2003	BS1: 1980--2003
France	No pacts		BS4: 1980--2003
Germany	No pacts; [2000]	[2000]	BS3: 1980--2003
Ireland	1980, 1987, 1990, 1994, 1997, 2000, 2003	1980--81; 1987--2003	BS1: 1980--2003
Italy	1983/84, 1992/93, 1998	1983--84; 1992--2002	BS1: 1980--84; 1986--2003 BS4: 1985
Netherlands	1982, 1986/87/88/89/90, 1992/93, 1995,	1982--90; 1992--97; 2002--03	BS1: 1982--2003 BS4: 1980--81

2002/03			
Norway	1980, 1988, 1992, 1998, 2003	1980--81; 1988--90; 1992--2000; 2003	BS1: 1980; 1983; 1985; 1987--2003 BS4: 1981--82; 1984; 1986
Portugal	1986/87/88, 1990, 1992, 1996	1986--88; 1990--92; 1996--99	BS1: 1982--2003 BS4: 1980--81
Spain	1981, 1984, 2001	1981--82; 1984--86; 2001--02	BS1: 1980--2003
Sweden	1985, 1990, 1995	1985; 1990-- 93; 1995	BS1: 1980--98 BS3: 1999--2003
United Kingdom	No pacts		BS2: 1980--2003 [BS1: 1980--83 BS2: 1984--2003]

Notes: * Including years of conclusion. Alternative coding of borderline cases in brackets. Sources: *European Industrial Relations Review*, *Euronline* (various issues), Fajertag (1996; 2000), Fajertag and Pochet (1997; 2000), Ferner and Hyman (1992; 1998), Hassel (2003; 2006), Mermet and Gradev (2002); Traxler et al. (2001), own data.

TABLE 2. The determinants of pacts

	PACTS/S				PACTS/C			
	(1) <i>Annual data (t)</i>				(2) <i>Periodized data (p)</i>			
	SC ⁺	AC ⁺	SC ⁺⁺	AC ⁺⁺	SC ⁺	AC ⁺	SC ⁺⁺	AC ⁺⁺
	(1a)	(1b)	(1c)	(1d)	(2a)	(2b)	(2c)	(2d)
C	0.1961 (0.1973)	0.1926 (0.1980)	0.3400* (0.1995)	0.3471* (0.2007)	0.1638 (0.6169)	0.1349 (0.6220)	0.7529 (0.6279)	0.8123 (0.6214)
UD _{t/p}	-0.0008 (0.0055)	-0.0007 (0.0055)	0.0007 (0.0056)	0.0004 (0.0056)	0.0217 (0.0199)	0.0218 (0.0201)	0.0230 (0.0190)	0.0202 (0.0192)
UD _t ² / _p	1.1E-05 (5.5E-05)	1.0E-05 (5.5E-05)	-3.5E-05 (5.9E-05)	-3.4E-05 (5.8E-05)	-0.0002 (0.0002)	-0.0002 (0.0002)	-0.0004 (0.0002)	-0.0004 (0.0002)
LEFTGOV _{t/p}	-0.0002 (0.0005)	-0.0001 (0.0006)	4.9E-05 (0.0005)	0.0001 (0.0006)	0.0007 (0.0017)	0.0012 (0.0018)	0.0012 (0.0017)	0.0019 (0.0018)
UPP _{t-1/p-1}	0.0169 (0.0095)	0.0177 (0.0095)	0.0232* (0.0099)	0.0244* (0.0100)	-0.0192 (0.0262)	-0.0136 (0.0268)	0.0093 (0.0301)	0.0194 (0.0307)
NPU	-0.0100 (0.0121)	-0.0091 (0.0122)	-0.0181 (0.0126)	-0.0179 (0.0127)	-0.0329 (0.0347)	-0.0310 (0.0352)	-0.0618 (0.0352)	-0.0647 (0.0356)
SEAEMU	0.0589 (0.0395)	0.0573 (0.0403)	0.0538 (0.0393)	0.0521 (0.0401)	0.0295 (0.1135)	0.0271 (0.1167)	-0.0382 (0.1155)	-0.0524 (0.1177)
RELULC _{p-1}	-	-	-	-	-0.0177 (0.0174)	-0.0157 (0.0177)	-0.0032 (0.0184)	0.0009 (0.0184)
CBI	0.0940 (0.0984)	0.1038 (0.0991)	0.0628 (0.0987)	0.0722 (0.0993)	0.2178 (0.3367)	0.3036 (0.3384)	0.0293 (0.3420)	0.0654 (0.3445)
GS	-0.0005 (0.0018)	-0.0006 (0.0018)	-0.0018 (0.0017)	-0.0019 (0.0017)	0.0034 (0.0050)	0.0025 (0.0051)	-0.0008 (0.0051)	-0.0021 (0.0050)
BD _{p-1}	-	-	-	-	-0.0021 (0.0027)	-0.0025 (0.0027)	-0.0017 (0.0027)	-0.0014 (0.0028)
PACTS _{t-1}	0.5279*** (0.0549)	0.5170*** (0.0542)	0.4849*** (0.0576)	0.4725*** (0.0568)	-	-	-	-

Bargaining Structure

BS2	-0.2184***	-0.2177***	-0.2814***	-0.2804***	-0.8140***	-0.8306***	-1.1418***	-1.1806***
	(0.0713)	(0.0716)	(0.0752)	(0.0753)	(0.1852)	(0.1919)	(0.2317)	(0.2311)
BS3	-0.3800***	-0.3806***	-0.4493***	-0.4521***	-0.6917***	-0.6711***	-0.8656***	-0.8453***
	(0.0691)	(0.0720)	(0.0744)	(0.0772)	(0.1784)	(0.1866)	(0.1859)	(0.1886)
BS4	-0.3256***	-0.3317***	-0.3743***	-0.3835***	-0.4300**	-0.4441**	-0.6532***	-0.7086***
	(0.0649)	(0.0651)	(0.0672)	(0.0675)	(0.1886)	(0.1822)	(0.2150)	(0.2117)
R^2	0.5871	0.5716	0.5962	0.5814	0.2940	0.2536	0.3422	0.3145
R^2 -adjusted	0.5710	0.5548	0.5790	0.5636	0.1648	0.1169	0.2106	0.1774
DW	1.9919	2.007	1.9722	1.9859	2.2178	2.2011	2.3607	2.3701
$N \times T$	320	320	319	319	85	85	85	85
F -test (all)	0.0000	0.0000	0.0000	0.0000	0.0143	0.0507	0.0044	0.0119
F -test (BS)	0.0000	0.0000	0.0000	0.0000	0.0000	0.0000	0.0000	0.0000

Notes: ⁺ Pooled TSCS analysis for models a and b. ⁺⁺ Fixed effects vector decomposition analysis for models c and d. OLS with panel-corrected standard errors in parentheses. SC: Standard coding, AC: Alternative coding, F -test: probability, $N \times T$: number of observations (missings excluded), DW: Durbin-Watson test. Reference category for BS = 'unpatterned' multi-employer bargaining (BS1). $**\alpha \leq 0.01$; $* \alpha \leq 0.05$. For variable definitions, see appendix.