

SOCIAL MARKET ECONOMY: A DISCURSIVE FRAMEWORK FOR  
EUROPEAN SOCIAL MODEL?

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Approval of the Graduate School of Social Sciences

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## **ABSTRACT**

### **SOCIAL MARKET ECONOMY: A DISCURSIVE FRAMEWORK FOR EUROPEAN SOCIAL MODEL?**

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The thesis mainly scrutinizes the evolution of European Social Dimension from the early period of the European integration to the Lisbon Summit of 2000 and the formation of the draft EU Constitution in 2003. While the focus is on the changing role of social policy at the European Union level during the period of welfare state transformation, the thesis tries to lay down the normative and discursive linkages constructed between the concepts of European Social Model and the Social Market Economy. Subsequent to the inquiry made into the theoretical foundations of the Social Market Economy and its practice in Germany, the thesis discusses how diverse European actors employ the concept, which is ambiguous in nature, as a comprehensive framework within which a European political identity that may be constructed around European Social Model could be grounded.

Keywords: European Social Model, European Social Policy, Social Market

Economy

## ÖZ

### SOSYAL PİYASA EKONOMİSİ: AVRUPA SOSYAL MODELİNDE SÖYLEMSEL BİR ÇERÇEVE?

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Bu tez temelde, Avrupa Sosyal Boyutu'nun Avrupa entegrasyon sürecinin ilk döneminden, 2000 yılında gerçekleştirilen Lizbon Zirvesi'ne ve 2003 tarihli Avrupa Birliği Taslak Anayasası'nın oluşturulmasına kadar geçen süreçteki gelişimini incelemektedir. Refah devletinin dönüşümü bağlamında, sosyal politikanın Avrupa Birliği düzeyinde değişen rolünü araştırırken, aynı zamanda Avrupa Sosyal Modeli ve Sosyal Piyasa Ekonomisi arasında kurulan normatif ve söylemsel bağlantıları açıklamaya çalışmaktadır. Sosyal Piyasa Ekonomisi'nin teorik temelleri ve Almanya'daki uygulamasının incelenmesini takiben, tez, çeşitli Avrupa'lı aktörlerin, yapısı gereği muğlak olan bu kavramı, Avrupa Sosyal Modeli çevresinde kurgulanmış bir Avrupa Siyasi Kimliği'nin yerleştirilebileceği kapsamlı bir çerçeve olarak nasıl kullandıklarını tartışmaktadır.

Anahtar Sözcükler: Avrupa Sosyal Modeli, Avrupa Sosyal Politikası, Sosyal Piyasa Ekonomisi

To my beloved grandparents

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## TABLE OF CONTENTS

PLAGIARISM .....	iii
ABSTRACT .....	iv
ÖZ .....	v
DEDICATION .....	vi
ACKNOWLEDGEMENTS .....	vii
TABLE OF CONTENTS .....	viii
LIST OF ABBREVIATIONS .....	x
CHAPTER	
1. INTRODUCTION.....	1
2. EVALUATION OF EUROPEAN SOCIAL DIMENSION: THE ROAD FROM ROME TO MAASTRICHT .....	11
2.1 Early Integration Period and Subordination of Social Policy to Economic Sphere .....	11
2.2 From Stagflation to Revival: The Period between 1970s and 1992 Maastricht Treaty .....	20
3. A NEW TURN TO DESIGN EUROPEAN SOCIAL DIMENSION.....	28
3.1 Welfare State Transformation in the Wake of Changing Economic Paradigm and Post-Industrial Transition .....	31
3.1.1 External and Domestic Structural Pressures: Globalization and the Changing Demography of Europe.....	32
3.1.2 European Integration and Operational Pressures: Single European Market & Economic and Monetary Union ..	35
3.1.3 New Social Risks in the Era of Post-Industrial Transition .....	39
3.2 EU Response to Welfare State Transformation; Modernizing the European Social Model .....	43



4.	SOCIAL MARKET ECONOMY IN THEORY AND PRACTICE.....	50
4.1	Examination of Social Market Economy from a Historical Perspective .....	53
4.2	Intellectual Roots and Institutional Foundations of Social Market Economy .....	56
4.2.1	Ordoliberalism and its Contribution to Conceptualizing Social Market Economy .....	57
4.2.2	The Contextualization of Social Market Economy by Alfred Müller-Armack .....	60
4.2.3	Critiques on the “Social” Adjective of Social Market Economy .....	65
4.3	“Social” Market Economy Theory in German Practice of Welfare State .....	67
5.	A EUROPEAN SOCIAL MARKET ECONOMY? .....	75
5.1	Assessing the European Social Model from the Perspective of “Social Market Economy” .....	77
5.1.1	The Feasibility or Otherwise of Establishing Social Market Economy Order for the European Union.....	79
5.1.2	Introducing the Social Market Economy Concept in the EU Political Discourse .....	82
5.1.2.1	The European Commission’s Perception on Social Market Economy .....	85
5.1.2.2	European Social Partners’ Perception on Social Market Economy.....	90
6.	CONCLUSION .....	94
	REFERENCES.....	101

## **LIST OF ABBREVIATIONS**

### ABBREVIATIONS

EEC	European Economic Community
EES	European Employment Strategy
EMU	Economic and Monetary Union
EPSU	European Federation of Public Service Unions
ESM	European Social Model
ETUC	European Trade Union Confederation
EU	European Union
OMC	Open Method of Coordination
SEA	Single European Act
SME	Social Market Economy
UNICE	Union of Industries of the European Community (BusinessEurope)

## **CHAPTER I**

### **INTRODUCTION**

This thesis mainly analyzes the prospect of “Social Europe” with respect to the recent endeavors of the European Commission to modernize the European Social Model and its incorporation of the concept of a “Social Market Economy” in the Draft Constitution in 2003 as well as the Lisbon Treaty of 2007.

The thesis has risen upon three building blocks. The first is about the historical progress of creating a European social dimension and introducing European Social Model into EU discussions. In this regard, the thesis examines the historical path within which European social policy has been developed and scrutinizes the reasons of bringing social sphere back into the European agenda in the early 1990s and accordingly modernizing the European Social Model. The European Commission has got involved more in organizing the social sphere of the European Union along with its attempts to modernize the European Social Model in the wake of new social risks stemming from the post industrial transition. This was evidently declared in Lisbon Summit of March in 2000 with a reference given to “becoming the most competitive knowledge based economy with greater social cohesion” (Euroactive, 2007).

The second building block of the thesis is about the theoretical foundations of Social Market Economy. There has already been a tendency among some politicians and scholars to concede the whole European welfare system as it exists within a kind of Social Market Economy. They often refer to the Social Market Economy as a European concept balancing market efficiency with social elements, which makes it ultimately different from the Anglo-Saxon type of capitalism led by the US. However, despite the fact that some political economies in Europe such as Germany, Austria, the Netherlands and Belgium may be regarded as variants of Social Market Economy, this tendency misses the point that there are still substantial differences among member states' welfare regimes. Therefore, there is an apparent need to clarify the precise meaning and foundations of Social Market Economy.

The third pillar of the thesis scrutinizes the cognitive correlation between Social Market Economy and European Social Model. In this regard, Jepsen and Pascual state that European Social Model is a political project comprising core values “through which a European identity might be constructed” (Jepsen and Pascual, 2005: 240). With reference to Social Market Economy concept, it is observed that the concept has been employed with various connotations in different contexts due to both its ambiguous nature and the changing political economy. Thus, there occurred to be more than one interpretation of Social Market Economy referred by scholar and politicians. In this regard, the thesis questions the perception and accordingly, the anticipation of the Commission and European social partners in

integrating the “Social Market Economy” concept in their discourses built upon the “European Social Model”.

It will be argued that, the importance of *discourse* should not be underestimated in building legitimacy of the welfare reform process. Schmidt and Radaelli define discourse in terms of its content “as a set of policy ideas and values, and in terms of its usage, as a process of interaction focused on policy formulation and communication” (Schmidt and Radaelli, 2004: 184). The argument set by Schmidt and Radaelli highlights the importance of discourse as “the discourse serves to enhance capacity by altering perceptions of problems and legacies and by influencing preferences.” (Schmidt and Radaelli, 2004: 186). Furthermore, Schmidt continues that:

Discourse matters but also when it matters, that is, when it acts as a causal influence on welfare reform, altering perceptions of interests and overcoming institutional obstacles to change. As both a set of ideas about the necessity and appropriateness of reform and an interactive process of policy construction and communication, discourse can create an interactive consensus for change (Schmidt, 2002a: 169).

In that context, the thesis aims to scrutinize the grounds of integrating the notion of Social Market Economy in the discussions revolving around “European Social Model”. Accordingly it inquires how Social Market Economy, on one hand constitutes one of the conceptual tools of building consensus in the social realm and constructing European political identity, on the other hand is presumed as a kind of normative baseline so as to propose it as an ideal model for European Social Model and/or to criticize the market-centered initiatives of the Commission. In this manner, this pillar conducts a two-pronged discussion with regard to the

ways in which Social Market Economy be used as moral fiber of the diverse arguments revolving around European social dimension.

It is also considered necessary to reflect the varying perceptions of the social partners in regard to Social Market Economy. Hereby, it is deemed essential to mention that although European Trade Union Confederation (ETUC) welcomed the Social Market Economy concept in the meeting on the European Convention, some of the social partners such as BusinessEurope (former UNICE) hesitated to use the terms Social Market Economy as it was considered as linguistically ambiguous.<sup>1</sup>

It is acknowledged that Social Market Economy is both associated with the economic governance, competitiveness and social objectives in the EU documents and the draft Constitution. However, the thesis will focus on the “social” aspect of the Social Market Economy in scrutinizing its relations to European Social Model.

The process of European integration initially commenced as a liberal economic integration project with a negligible component of social policy and gradually evolved to a Union entity affecting the socio-economic structures of its member states as well as influencing the very daily lives of its citizens. However, from the very beginning of integration, the progress in the economic sphere leading to gradual convergence has not been accompanied with the parallel developments in

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<sup>1</sup> The statement made by both ETUC and the UNICE were recorded in the “Notes of the Meeting of The European Convention, 6 and 7 February 2003” [http://www.epin.org/new/files/report\\_12.pdf](http://www.epin.org/new/files/report_12.pdf)

the social dimension, that is to say, European social dimension lagged behind economic advancements.

Its conception as a liberal economic project has been reflected with the setting of the principle of “open market economy with free competition” as stated in its founding Treaty in 1957. This integration pattern generated a continuing process of convergence in economic policies at the European level which started with the aim of establishing a common market and fostering economic advances. In due course, this paved the way for the European integration process, to an important extent, to be driven by economic initiatives. No obligatory binding legal framework, however, has been drawn up for the harmonization of national social policies at the European level; and the diversity in national social policy and welfare arrangements has, to a large extent, persisted. In other words, the social dimension was given a secondary role compared to economic integration and the initiatives on this policy domain remained with the member states.

In this context, the social and labor market policies mostly remained a national concern. However, as the European integration intensified following the establishment of the European Single Market and subsequently the Economic and Monetary Union (EMU), the room for national member states to design their socio-political agenda has gradually limited. According to Scharpf; “The capacity of national Member States to determine the course of their own economies, henceforth, to realize self-defined sociopolitical targets has been bounded” (Scharpf, 2002: 648).

The impact of European economic integration process on national welfare states' policies deepened in line with external and internal pressures transforming welfare states such as economic globalization; intensified international competition, technological advancements and demographic factors such as ageing population. Public concerns regarding the neo-liberal character of economic and monetary policies which might endanger the subsistence of traditional so-called European labeled Social Model have increased. In accordance with what Karl Polanyi described as "double movement", the European open market formation - intensifying in the era of globalization- would be responded with self defending "countermovement of society" so as to "protect itself against the perils inherent in a self-regulating market system" (Polanyi, 1944: 76). In due course, fostering the advancement in the European social sphere together with economic growth has become crucial in order to fill the probable social deficit of the European Union and lessen the public discontent for further European integration. Hence, in the wake of the changing economic conjuncture in the 1990s, the EU has sought to become compatible with international competition and increase its economic growth, while aiming to create the 'Union of people' with more social cohesion.

The late 1990s and early 2000s experienced a new phase of EU-led initiatives at the social field. Accordingly, the European Union, encompassing different welfare regimes, has developed new methodologies and strategies so as to become compatible with growing international competition and to balance social demands to achieve its constitutional foundations. Endeavors to adapt social and labor market policies to the latest internal and external pressures and to confront new



social risks brought about new discussions on modernizing –or even questioning the existence of- the European Social Model.

European Union, therefore, has sought to become the resort of mediating these challenges on the European level, while ensuring the success of the Internal Market. In the Lisbon Summit of March 2000, the EU ambition to cover the social field and to deal with the current unemployment and competitiveness problems has become more evident.

At this juncture, the Lisbon Agenda highlighted the importance of modernizing the European Social Model in the wake of socio-economic changes. European Social Model, initially incorporated into the EU discourse by Delors, is characterized with economic prosperity, generous welfare arrangements and extensive participation of social partners. Jepsen and Pascual states that European Social Model terminology was first popularized during the Delors's Commission as an endeavor to “designate it as an alternative to the American form of pure-market capitalism” (Jepsen and Serrano Pascual, 2005: 234). The main starting point, with regard to modernization of the European Social Model, was preserving the “traditional features” of so-called European labeled Social Model while revisiting these foundations in line with current requirements of the global economic order and rising new social risks. These merging practices are articulated as ‘modernizing’ the European Social Model, in the discourses of the European Commission, as it might be considered a meeting point of neo-liberal understanding of political economy with more traditional concerns underlining the need for social cohesion. Re-pronunciation of

the term in both EU discourses and academia is seen as a European response to changing economic conditions and the reflection of the attempts to relocate the European systems of welfare in accordance to post-industrial transition.

Following the Lisbon Summit, the European Commission announced to “work for a Social Market Economy”, aiming to balance market outcomes with social elements, in its draft Constitution in 2003. The statement of the EU to work for highly competitive Social Market Economy is repeated in the Treaty on Functioning of the EU –Lisbon Treaty, The Treaty which is an amendment to the previous Treaties was signed by the heads of state and governments of 27 Member States and is still waiting for the ratifications of all member states (Council of the European Union, 2007). Thereby, the thesis scrutinizes the correlation between the efforts to modernize the European Social Model and the introduction of the Social Market Economy notion and discusses the European Social Model from the various European actors’ perspective of working for a Social Market Economy. The thesis is organized along the following chapters:

In the first chapter, a brief overview of the history of European social policy is made with the aim of providing a historical background. Here, the reasons of subordinating social policy to the economic sphere are explored.

Second chapter examines the motives behind the changing attitudes of the European Commission in the social sphere following the 1990s. Therefore, the efforts to modernize the European Social Model are scrutinized. Thereby, the

perception change of the Commission regarding the role of the social policy-for being a “productive factor” rather than “by product of economic policies” and prioritization of employment policies is elaborated. In due course, the new initiatives at the European social sphere such as establishing OMC and EES are scrutinized.

Subsequent chapter explores the concept and history of Social Market Economy in order to evaluate the European social model vis-à-vis the notion of ‘Social Market Economy’. At this juncture, the history of conceptualizing Social Market Economy, its roots, and founders and its practice in Germany is scrutinized seeing that analyzing the relevance of the concept at the European level necessitates a considerable inquiry into its precepts along with its historical in Germany. It is stated that the Social Market Economy model which was originated and implemented in Germany after the Second World War should not be considered only as a solid concept with clear-cut notions but be taken as a process effected by both German socio-economic institutions and political economy of the era. Finally, the fundamental features and institutions of Social Market Economy are elaborated. Most importantly, all through its history Social Market Economy has been redefined and employed with different connotations in line with changing economic and political structures. This generated a divergence from the original theoretical foundations and gave rise to explanations of the Social Market Economy concept varying in content. For that reason, the direction within which the Social Market Economy model has evolved in the historical process is examined.

In the fourth Chapter, the new role adopted by the European Commission in mitigating the new challenges and promoting policy reform in line with new social risks emanating from changing economic and political conjuncture is studied. In order to promote this policy reform, the Commission has generated *discursive framework* general enough so that the policy groups can subscribe and adapt to it as well as inclusive enough and intimate with the policy aspirations of the majority of the Council and the Parliament. This discursive framework is the notion of the Social Market Economy, ambiguous as it has deployed with various connotations all through its history. Accordingly, the thesis investigates, to what extent, the Social Market Economy theory could be utilized as a comprehensive discursive framework within which the endeavors to modernize European Social Model could fit in. The thesis aims to state how the incorporation of the Social Market Economy concept has served to increase the role of the Commission in the European integration process by means of generating a European discourse.

The thesis finalizes with a conclusion chapter where summary of the main findings is given.

## **CHAPTER II**

### **EVALUATION OF EUROPEAN SOCIAL DIMENSION: THE ROAD FROM ROME TO MAASTRICHT**

This chapter scrutinizes the reasons behind the changing role of social policy and industrial relations at the EU level especially starting with mid 1990s. First, the history of European integration and conjuncture of the postwar era will be discussed so as to clarify the bases of subordinating social policy considerations to economic prerogatives. Secondly, a broad-scale picture explaining the reasons of reinvigorating a pan-European social dimension in the Union after the signing of the Single European Act (SEA) is tried to be drawn. Hereby, the international economic and political environment of the time is taken into consideration to account for the emergence of a long-lasting debate regarding the European Union's social dimension.

#### **2.1 Early Integration Period and Subordination of Social Policy to Economic Sphere**

After the devastating Second World War, Western European States agreed upon a new initiative aimed at creating a peaceful environment and ever closer union where European national states could cooperate and improve the economic performance as well as disseminating prosperity throughout Europe.

European integration process has been elaborated by different theoretical approaches. Mainstreaming views stated that this integration process has been initiated to bring peace to the Europe Continent as it would impede international war and hostile economic rivalries among national states. This would be realized via tying core industrial sectors and subsequently economic interests of national member states by means of establishing a common market. Accordingly, this initiative would increase and disseminate economic and social well being of these countries. Some scholars, on the other hand, deemed that the initiative mostly evolved to a project aimed at rebuilding Western European economy and extending internal market while serving for economic interests of nation states. As Moravcsik argues, “rational national states first and foremost guarded their core economic interests and EEC emerged as a result of following rational decisions made by member states in pursuit of core economic interest” (Moravcsik, 1998: 1). Accordingly, it was primarily focused on economic issues and liberalizing markets via eliminating trade barriers, tariffs and finally establishing common market. Offe divides the interpretations concerning the process of integration as optimists and pessimist readings. Accordingly, the “optimistic” reading (Offe, 2003: 447) of the European integration project deemed that corollary to this integration process, “supranationally embedded political economy would serve the interests of all parties involved evenly”. The critical reading of the European integration project (Offe, 2003: 447) further reckoned that European integration would lead to the “ultimate triumph of market liberalism on the European Continent by enforcing upon member states the adoption of regimes of privatization, deregulation, and

fiscal austerity.” Martin and Ross summarize the causes behind the economic integration as “the economic approach was adopted because it seemed the only way to generate the necessary political support. But this approach meant that integration had to be consistent with the economic interests whose support was decisive, primarily European capital and national governments” (Martin and Ross, 1999: 314).

In brief of theoretical discussions, it can be stated that the European integration process was pioneered by economic integration and this integration pattern has remarkably generated common economic institutions. The process was provided with market-making measures firstly before developing market-correcting means. Thereby, social policy was given a minor role in the integration process and the responsibility for market-correcting was, to a large extent, remained with member states.

In light of this argument, subsequent to further economic integration, member states have been steadily bound with common economic criteria, in particular hard law provisions aiming to encourage unity in action, with the aim of establishing a common market and gradual convergence on economic policies, whereas they have maintained their national competencies on social policy domain and requested only to cooperate on social dimension.

Social issues were mostly touched upon under the provisions arranging the free movement of workers, services, capital, and goods. Still, some articles in the Rome

Treaty directly stipulate the action at the issues at social field. For instance, EEC Treaty, Article 117 stated that “Member States agree upon the need to promote improved working conditions and an improved standard of living for workers” and it continues with the statement saying that “so as to make possible their harmonization while the improvement is being maintained” which foresees the harmonization of the social systems as the integration proceeds. Moreover, the Article 118, gave the Commission the task of promoting close cooperation between Member States in the social field such as employment, labor law and working conditions and social security (Eurofound. a). In addition, Treaty establishing EEC integrated some other fundamental employment and social policy concerns into their provisions without providing them with a binding character. These were the statements foreseen in Rome Treaty such as equal pay between man and woman and institutionalizing Euro-corporatism in the Economic and Social Committee and creation and operation of European Social Fund (Geyer, 2000a: 246). However, these provisions were mostly designed to complete the formation of labor market as well as for the sound functioning of common market. For instance, European Social Fund (article 123-128) were designed to respond to the need of improving labor’s “geographical and occupational mobility” while providing financial means through vocational training and retraining (Manow, Schäfer and Zorn, 2004: 19). It also aimed at supporting and improving industrial change throughout the Community (Ibid: 19). Overall, as Geyer pointed out “the EU social policy was slow to develop and limited to its foundations in the treaties in spite of the efforts of the Commission, parliament and trade unions to spread out the area for social policy and boost the importance of social policy relative to economic issues”



(Geyer, 2000b: 26). By the 1990s when the Unions competence on social policy increased, earlier provisions on workers' right and welfare benefits became an important part of the debate surrounding the future of European integration.

The secondary role and subordination of social dimension to the economic progresses might be argued to rise upon three interwoven facts. At first place, the geopolitical distress in the wake of Cold War and international conjuncture of the time as growing systems of competition influenced the form of the integration via importing economic and security concerns to the European agenda. In 1947, the international economic cooperation intensified with the operation of IMF and World Bank and took a step further with the negotiations for free trade in General Agreement on Tariffs and Trade (GATT). European national states played their role in the GATT negotiations; however they felt the need of creating specific West-European based economic initiatives (Nugent, 2003: 15). Besides, the influence of USSR on domestic communist subversions in Western European countries following the emergence of Cold War cultivated the endeavors of the European national states to establish close collaboration with United States so as to settle on their position in the rigid bipolar world (pdseuropa). This close cooperation with the US was augmented with the European Recovery Program known as Marshall Aid generating economic and political inter-dependence among European states which facilitated the process of initiating an economic integration among the them (Hörber, 2006: 305).

Secondly, the period of economic integration coincided with Keynesian compromise, otherwise referred to as regulated nature of “embedded liberalism” (Ruggie, 1992). National states had the chance to develop different systems of economic management and welfare under the “protective barriers of capital exchange control, fixed but adjustable exchange rates and optional barriers to trade” during the international regime of embedded liberalism. Accordingly, the degree of business interconnectedness, government intervention and labor cooperation has changed in varying degrees (Schmidt, 2002b: 147). Between the years of 1945 to 1970s, Keynesian demand management seemed successful in ensuring high economic growth and balancing the costs of a prolonged expansion in welfare services. As Geyer indicated, “the success of social policy developments at the national level made European social policy creation redundant and robbed it of its political supporters” (Geyer, 2000b: 32).

Most importantly, as the integration continued and more national arrangements with diverse welfare state became members of the Community, the welfare state provisions, to a large extent, diverged at the EEC level. It became evident at a time when the first enlargement round. Along with the inclusion of three new member states in 1973 two of which, the UK and Ireland, are typified as liberal welfare states by Esping Andersen compared to six founding states whose welfare state formulations were distinctive from liberal welfare state with respect to their corporatist and conservative configuration of socio-economic institutions (Scharpf, 2002: 646). As a matter of fact, the varieties of welfare states and different social

systems prevailing throughout Europe have constituted one of the factors which slowed down the process of harmonizing social systems.

Thirdly, the influence of the European elites and the approaches of national governments and national party politics to the European integration have also influenced the social policy development at the European level. At the beginning of the integration, it was mostly considered that, as the economic integration succeeded, greater social benefit would follow. In other words, social dimension was perceived as “by product” of economic progress, when it is assessed from a neoclassical framework (Geyer, 2000a: 246). For instance, in the Rome Treaty, Article 117 stated that “functioning of the common market will favor the harmonization of social systems”. This statement in the constituting Treaty could also be correlated with the discourses of neofunctional approach which was the dominant integration theory of late 1950s and early 1960s and was considered as successfully descriptive of the period (op.cit). Geyer, by referring to Haas, states that according to the “expansive logic of integration through spill over” the primacy should be given to economic issues. Subsequently, the benefits gained from the economic integration would spread to other policy areas, and then social policy and other policies would follow the path of economic integration (op.cit).

However, the empty chair crisis in the mid 1960s and De Gaulle’s opposition to supranationalism hampered further surrendering of the national competences to the supranational level in other policies as it challenged the belief in “the power of the integration dynamic” (Dinan, 1999: 3). The influence of political environment and

party politics over community initiatives became more apparent. Intergovernmentalism approach highlighted the influence of national governments in Community policy making. Accordingly, more emphasis was made on the preferences of member states' governments as it is deemed that their decisions shaped the major developments in the European integration process. The dependency of Community to political environment has also influenced the political climate within which the Community functioned over the next years (Ibid: 49). In due course, government politics in member states have affected the positioning of social policy in the integration process, therefore have had an impact on the development of European social dimension. Besides, for the early period of integration, it is mostly accepted that the difference between moderate parties, the left and right of the center, with regard to integration was not very significant. Consequently, the vast majority of these parties had implicitly agreed on limiting the further competence transfers to the EEC level despite the fact that the parties in governments had distinct attitudes regarding social policy issues, (Manow, Schäfer and Zorn, 2004: 19).

Even though the theoretical approaches which try to explain the path of European integration have differed, the position towards social policy, to a large extent, remained identical in terms of giving the social policy a secondary role (Geyer, 2000b: 32). As Geyer points out; the essential potential of social policy was emphasized by the neofunctionalist approach since it is believed that as the benefits of European cooperation and integrating expanded, more and more economic and social problems and policies would be transferred to the European level. However,

intergovernmentalism gave it a secondary role “not because of its essential potential but because it was a minor side issue and used to assuage doubts and buy serenity.” (op.cit.).

When it comes to late 1960s, subsequent events induced European community to discuss the social dimension and cohesion capacity of the Community. The distribution of the benefits of the economic boom of postwar years was interrogated during the events of “Paris Spring of 1968” as many groups were still excluded from the labor market (Kenner, 2003: 24). Besides, the bloom of economic growth of the postwar years started to fade and unemployment rate was rising accordingly (Tsarouhas, 2007: 22). Therefore, integrating social issues in the Community agenda happened to be more substantial. In 1969 Hague European Council, German Chancellor Willy Brandt emphasized the need to producing a “human face” for the European integration by means of coordinating economic integration with social harmonization (Kenner, 2003: 24).

As it was discussed above, the European integration project had been designed and driven mostly by the European political elites. However, as the integration proceeded, the European political elites felt the necessity to incorporate all segments of society into integration process so as to demonstrate that economic integration is not an end itself. This could be better achieved by covering social policy area; however, the disinclination of the national member states to transfer their competence hampered the process of establishing the European level social policy (Tsarouhas, 2007: 22).

## **2.2 From Stagflation to Revival; The Period Between 1970s and 1992 Maastricht Treaty**

In 1970s, the initiatives to organize social field in the Community became more tangible along with the Paris Summit of 1972. In the event, the need to enhance the social dimension was put forward. This has been followed by the introduction of Social Action Programs which can be considered as a solid outcome of the emphasis made towards formulating more concrete European Social Policy for the first time by the Members. Accordingly, the first Social Action Program of the European Community (SAP) was implemented in 1974. Social Action Program laid down the political targets as full and better employment, improvement of working and living conditions and greater participation of workers and employers in the economic and social decisions of the Community (Kenner, 2003: 24).

In spite of the increased demands for the EC policy in the aftermath of 1974 Social Action Program, the limitations in international environment and the form of SAP as it was introduced in a form of influential but no binding soft law (Kenner, 2003: 24) prevented the conversion of the provisions into the European social policies (Geyer, 2000b: 38). Late-1970s were the era of stagnation reflected in the progress of development in the social policy field. The employment target in the Social Action Program could not be attained in a period of economic downturn. In addition, the economic recession of 1973 and 1979 was tried to be surmounted with the autonomous economic strategies of national states. These autonomous economic policies of member states forestalled the endeavors to enhance the social

dimension of the Community (Tsarouhas, 2007: 23). As a result, developments in European level social policy were limited to some specific areas. In Geyer's words, "attempts at creating more substantial social rights, particularly in the areas of labor rights and participation were blocked, diluted or abandoned" (Geyer, 2000b: 40).

The confederalist approach asserts that nation-states exist within the web of interdependent economic, political and social relationships might decide to generate "long-term co-operative and integrative strategies", not necessarily permanent, to facilitate their operation within the web of interdependence. Consequently, they interpret that this fragile cooperation among the nation states could be hampered by international factors and national developments. European social policy has followed an indecisive path of development shaped with the dynamics of European integration (op.cit).

Kleinman listed three reasons behind the limited progress in the field of the European social policy. First, the opposition of new British government of Margaret Thatcher curtailed the further development of Action Plans as they interpreted such initiatives for being a factor increasing labor costs and creating rigidities in the labor market. Secondly, the political atmosphere shifted towards Right and Center Right among the governments of member states. Finally, there emerged a contention regarding the "competitive disadvantage" both within the EEC countries and their relation to the rest of the world. (Kleinman, 2002: 86).

In brief, the economic situation of the time and the political attitudes created its own dynamic that faded the possibility for advancing Community level social policy (Manow, Schäfer and Zorn, 2004: 19). However, in the second half of 1980s, the European integration was revitalized and developments in the European social policy have followed the same path. The introduction of Single European Act in 1986 invigorated the attempts to organize the social field at the European level although its main goal was the completion of Single European market. Furthermore, the influential political actors of the time such as Mitterand and Delors with Chancellor Helmut Kohl of Germany were more activists in terms of activating further progress in the social policy and endeavored to accelerate the European integration while generating an amalgamation of economic integration with social aspects. Having concentrated on enhancing the human face of the integration, these political figures all concurred with the need to deepen the “social dimension” of Europe. After experiencing the international recession and soaring unemployment, social policy making mostly focused more on the employment problem.

The need to develop the “social dialogue and cooperation and consultation over social protection” so as to become more comprehensive with regard to including social partners is stated (Kleinman, 2002: 87). Besides, according to Bornschier and Ziltener; union dynamism which came with the convergence of unions’ EC policies and their successful mobilization as well as Delors encouraging approach to social partners was formed the bases of endeavors to enhance social dimension at the EU level (Bornschier and Ziltener, 1999: 45). In due course, the role and the



importance of social partners in the process of social policy making were highlighted by the leading figures of the time, to some extent, with the aim to decrease the tension upon European integration for being an elitist project.

The idea of enhancing the social dimension of the European integration in line with the completion of internal market further stimulated the initiatives in supporting and enhancing the social dialogue at the EU level. The call for the Val Duchesse meeting in 1985 was the initial attempt of constituting a formal European level social dialogue. In Val Duchesse meeting all the national organizations that were the members of UNICE-Union of Industrial and Employers' Confederations of Europe-, CEEP-The European Centre of Enterprises with Public Participation- and ETUC -European Trade Union Confederation- were gathered together to negotiate the issue of European social dialogue. The success of the negotiations was the introduction of the European social dialogue by the Single European Act 1986 of a new Article 118B (Eurofound. b).

The Single European Act signed by the twelve member states in 1986 was the major revision for the EEC treaties and stipulated new decision making process. Accordingly, the European Community's powers in social policy were extended. The qualified majority voting was extended to health and safety of workers with a new article amending Article 118 of the Treaty. As stated above, the Article 118B opened up the ways of developing social dialogue at the European level. There, it is stated that "The Commission shall Endeavour to develop the dialogue between management and labor at European level, which could, if the two sides consider it

desirable, lead to relations based on agreement” (Eurofound. c). As Tsarouhas indicates; “The signing of the Single European Market marked the history of European integration process as it provided extensive stipulation for further integration and a moving beyond the intergovernmentalist perspective” (Tsarouhas, 2007: 25). During the Belgian presidency in the second half of 1987, the idea of a social dimension within the SEM was put forward. This idea was further strengthened in European Council meeting in Hanover 1988 with a statement that the provisions for internal market should not lessen the degree of social policies in Member States (Bornschier and Ziltener, 1999: 44). President of the Commission, Delors pointed that there was a need to revive social policy which includes a minimum platform of rights along (Kelinmann, 2002).

All the efforts set up for the European social dimension starting from 1985 was articulated in the Community Charter of the Fundamental Social Rights of Workers. In December 1989, the heads of eleven out of the twelve member states, except United Kingdom, signed the Community Charter of the Fundamental Social Rights of Workers, namely the Social Charter. Thatcher government in the UK opposed to extend social dimension with respect to their hesitation for more supranational actions taken at the European level. Eventually, The Social Charter became a legally non-binding “solemn declaration” (Kenner, 2003: 512). Having focused on the “workers” rather than citizens, The Charter prioritized labor and workers’ rights. However, it offered an impetus for the developments of the social rights not only in the internal market but in the overall social sphere at the European level (Adnett and Hardy, 2005: 6).

The revitalization of the European integration process, triggered with the signing of the Single European Market Act, has entered another phase with the introduction of the economic criteria for the establishment of Economic and Monetary Union (EMU) in the Maastricht Treaty- establishing the European Union- in 1992. EMU would “introduce a single currency replacing the national currencies and would be managed by an independent European Central Bank whose primary object is price stability” (Martin and Ross, 1999: 319). The Treaty establishing the EU brought about new provisions for regulating the European social sphere.

In the EC Summit in Maastricht, eleven member states, aside the UK, decided to continue on the path drawn by the Social Charter and to finalize it with a Protocol on Social Policy (Bornschier and Ziltener, 1999: 46). Hereby, European social partners played a crucial role in the negotiations at the Maastricht which led to the signing of Maastricht Treaty establishing the European Union. The Protocol incorporating an Agreement on Social Policy was attached to the Maastricht Treaty with few modifications and British opt-out. The UK was given an opt-out for the Agreement on Social Policy which ended in 1997 with the election of the British Labor’s Party. The so-called Social Agreement dealt with both social policy content and policy making procedures as it broadened EU competence in social policy and provided a particular procedure for European social dialogue (Eurofound. c). Subsequently, three levels of social partner participation in policy process were introduced by the EC Treaty’s social provision. First, the obligation of the Commission to consult the both side of the industry before submitting social policy proposals has been included. Secondly, it was stipulated that member states

may delegate management and labor within the process of implementing of the Directives adopted in accordance to Social Agreement. And according to Falkner, “most importantly, management and labor may, on the occasion of such consultation, inform the Commission of their wish to initiate negotiations in order to reach agreements instead of traditional EC legislation. Such agreements may, at the joint request of the signatory parties, be implemented by a Council decision on a proposal from the Commission” (Falkner, Hartlapp, Leiber and Treib, 2002: 4). This three layer procedure for the European social dialogue founded the bases of future European Union wide collective agreements (Adnett and Hardy, 2005: 6).

The unanimity requirements for the social policy had caused social dimension lagged behind the economic integration. Nevertheless, the EU Treaty expanded the areas where majority voting can be applied such as working conditions, information and consultation of workers, equality between men and women, integration of excluded people from the market (Falkner, Hartlapp, Leiber and Treib, 2002: 3). However, unanimous vote of the eleven (later 1995, fourteen) were required in the areas such as social security and social protection of workers as well as representation and collective defense of interest of workers and employers (Bornschier and Ziltener, 1999: 46).

Overall, the signing of Maastricht Treaty was significant in terms of gathering economic and social concerns together by setting economic targets; criteria for Economic and Monetary Union and incorporating a Social Agreement with extended EU competences on social policy to the body of the constituting Treaty.

As it was indicated above, the developments at the European social dimension have followed the dynamism of the integration. As the Single European Act gave an impetus to the integration process, the attempts to enhance the social aspect of the European Union was taken to the agenda of the European political leaders, especially in company with the Delors's vision for Social Europe. However, the introduction of EMU and the priority given to the binding criteria for establishing an Economic and Monetary Union and continuing reluctance of the member states, namely the UK, to give competence to the EU on the social issues overshadowed the attempts of creating a comprehensive European social agenda.

Along with the reasons counted in the next chapter, covering the social sphere gained a new pace, especially by the late 1990s and early 2000s. New expansions brought into the European agenda by mid 1990s especially in regulating the employment policies which is incorporated to the Amsterdam Treaty in 1997 and subsequently social sphere. In the EU pronouncement, with the Treaty of Amsterdam "the policy for the promotion of employment finally moved to the top of the agenda, becoming a matter of common interest".<sup>2</sup> Heretofore, the "European" Social Model notion has re-entered into the discourses of both the European institutions and the social partners.

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<sup>2</sup> For more details; Employment and social policy, <http://europa.eu/scadplus/leg/en/s02300.htm>

## **CHAPTER III**

### **A NEW TURN TO DESIGN EUROPEAN SOCIAL DIMENSION**

In this chapter, the grounds of amplified focus of the EU on the European social dimension as well as the changing perceptions of the European Commission with regard to the role of the European employment and social policy is tried to be explained. Accordingly, this chapter explores how the Commission, got involved in organizing the European social sphere with the aim of adjusting the existing socio-economic structures of the so-called “European Social Model” to the conditions of changing political economy.

The reasons behind the increased engagement of the European Union in organizing labor markets, employment and social policy starting from mid 1990s, could be counted as follows: First of all, the changing economic paradigm, the shift from Keynesian compromise to neo-liberal restructuring, starting from late 1970s and intensified in 1990s and changes in demographic indicators and gender relations have induced both member states as nation states and the EU as a comprehensive entity to take feasible measures and define new social policy arrangements in order to mediate the problems resulting from the transformation of welfare state which undermine the existence of so-called European Social Model. Moreover, the role of national member states in welfare policy development at post war era has been challenged in line with the process of globalization combined with the European

integration (Hay, Watson and Wincott, 1999: 6).<sup>3</sup> As the national states are bound up with the economic criteria of the European integration, their capacity to design their own socio-political agenda has gradually decreased, however their reluctance to give competence to the EU in the social policy field has to a large extent persisted.

As a result of this empirical and/or of “perceived” challenges, intensification of the international competition and changing labor market structures urged European policy makers to tackle the current competitiveness problem and to produce new governance methods, namely Open Method of Coordination (OMC), while creating strong linkage between being competitive and socially inclusive. As Sapir indicates, the economic insecurity that arises from the unsolved challenges in the wake of increased competition is considered as a threat for the European integration project (Sapir, 2006: 370).

Second reason behind the EU’s increased involvement in the social sphere is to maintain the popular support for the European integration project, which necessitated to develop policies in order to decrease the costs of creating integrated “continental economy” and a single market in Europe (Kleinman, 2002: 86). Social deficit of the EU became more visible along with the conviction among the scholars and the economist that the further economic integration lacking social

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<sup>3</sup> Hay and his colleagues indicate that “Globalisation and European integration are not easily disentangled. For, whilst a number of authors see regionalisation and globalisation as sharply antithetical processes, others effectively conflate the two, treating, for instance, deepening regional economic integration in Europe as evidence itself of global economic integration.” (Hay, Watson and Wincott, 1999: 6)

correction at the EU level would lead to mount the negative consequences of international competition.

Thirdly, the increasing commitment of the trade unions and leftist parties and their growing role in the development of social dimension has become evident (Geyer, 2000b: 47). According to the Taylor-Gooby,

Center-left governments predominated in the main EU member states in the late 1990s, a new approach to social policy was sought which avoided both the traditional EU approach of European centralized state-building and an uncoordinated neo-liberal agenda of competition at the level of welfare regime (Taylor-Gooby, 2004: 187).

Besides, further involvement of European social partners in the integration project has become essential with a view to create new allies for the future Commission led initiatives (Wahl, 2002). Subsequent to the signing of Maastricht Treaty, the European social partners have become more influential in determining the scope of the social policy provisions and increased their future involvement along with the joint proposal on “future involvement of the social partners” submitted to Intergovernmental Conference and integrated into the EC Treaty’s social provision with minor changes. New provisions on social dialogue made it possible for the negotiated agreements to become “binding substitute for legislation”. Therefore; the social partners have become “formal co-actors in EU policy making” with the encouragement of the Commission (Falkner, Hartlapp, Leiber, Treib 2002: 3).

Above and beyond, the influence of the ETUC as a social partner has been enhanced following the initiatives of the Delors’s Commission to make the social dialogue work at the European level through strengthening the pose of the ETUC



via providing it the necessary resources (Martin and Ross, 1999: 324). Besides, a stronger ETUC, mostly relying on the resources of the Commission would cooperate with the Commission in essential political matters. Along with the efforts of the Commission, other European institutions, namely the Parliament, encouraged the empowering of the ETUC by “establishing a line in the 1989 budget to give ETUC new technical capacity.” (Martin and Ross, 1999: 326). Besides, the Parliament supported the intensification of the sectoral-level trade union structures, to organize worker representatives in the multinational corporations. Accordingly, European institutions’ supports reinforced the diverse organizational components of the ETUC (Ibid: 326-327). Overall, the influence of trade unions in the design of European Social Model has, to an important extent, increased.

### **3.1 Welfare State Transformation in the Wake of Changing Economic Paradigm and Post-Industrial Transition**

The reasons behind transformation of welfare states arrangements might be compiled under *structural* and *operational* pressures triggering welfare state transformation. The structural pressures could be divided into two as external structural pressures and domestic structural pressures. While demographic indicators such as aging populations and dramatic changes in the structure of household practices could be considered as domestic structural challenges, the globalization and its attendants are mostly counted as the external structural pressures.

### **3.1.1 External and Domestic Structural Pressures: Globalization and the Changing Demography of Europe**

Regarding domestic structural challenges, imminent population aging and changes in household practices and de-industrialization are among the internal challenges constraining the traditional functioning of national welfare states. Fall in birth rates as well as increase in the numbers of aged population produced the ageing problem of the society. As a result, the ratio of pensioners to workers increased considerably which constitutes substantial demand for social security and increased the weight of existing pension system. To be more tangible, aging population and unemployment of low skill workers as a result of emergence of high-technology oriented professions and more service based economy have constrained the funding of welfare state provision, thus, put burden on the implementation of social protection schemes and imperiled the sustainability of social security systems. In this regard, Pierson claims that

The budgetary stress on welfare states is primarily related to a series of post-industrial changes occurring within advanced industrial democracies themselves, as the employment profiles of affluent societies have become increasingly service-based, as their welfare has matured, as populations have aged, and as radical changes in household structure have taken place (Pierson, 2001: 82).

Some scholars assert that post industrial changes would culminate in welfare retrenchment According to Taylor-Gooby, “social needs generated by industrialism and centered on interruptions to family wage are facing pressures from different directions” (Taylor-Gooby, 2004: 5). On the contrary some argue that these post-industrial changes would bring about the expansion of welfare state. According to Iversen, both government consumption of services and social transfers as shares of

GDP have risen sharply and almost without interruption since 1950s, although the very rapid expansion beginning in the mid 1960s slowed down somewhat in 1980s. But there are no signs of any broad-scale retrenchment of welfare state (Iversen, 2001:45).

The Golden Age, a period which refers to the prosperity years after WWII with higher degrees of profitability and employment, had come to an end in mid 1970 along with the collapse of Bretton Woods system and the oil crises of 1973 and 1979. Accordingly, the end of Keynesian compromise and the structural crisis of mid 1970s and early 1980 have paved the way for the rise of neo-liberal policies in advanced capitalist countries. For that reason, starting from early 1990s; world economy has entered a new phase of intensification of international competition and increased capital mobility along with the new generation of high technology usage in advanced capitalist countries. This period was named "globalization" and soon became a part of scholarly debate and daily life of people in early 1990s. Although there is not a clear and concrete definition of the concept, it is mostly regarded as the greater connectedness among economies, politics and cultures or intensified social-economic networks, internationalization of capital which supported by technological evolution and which is expected to gather the world in one single unit (Giddens, 1990).

The transformative impact of globalization on national welfare state arrangements are discussed from different scopes and its effect varied according to different approaches. Ellison defines three extensive categories of varying approaches to

globalization in terms of its influences on the transformation of welfare state (Ellison, 2006: 48). Globalization skeptics regard the welfare state transformations more as an issue of endogenous economic factors like unemployment, low growth, changing gender relations and ageing population, than as merely a consequence of global economy. Middle way arguments regard global economic changes have significance, but not much significant in welfare regime transformations as enthusiasts believe (op.cit). The scholars that hold this view connote that, countries' have the ability to cope with global challenges by means of institutional adjustment, which does not essentially change their character (Ellison, 2006: 49).

Finally, the group of scholars contending that globalization substantially produced transformative pressures on national welfare states settlements might be divided in two categories, the optimists and the pessimists with regard to their assumption of the potential consequences of globalization on welfare state transformation. The pessimists constitute the majority and they argue that globalization may result in a crisis and retrenchment of the welfare state (Scharpf 1992, Rhodes 1996). The optimists hold that the contemporary welfare state may be compatible with globalization and this may even result in an expansion of the welfare state (Brady, Beckfield and Seeleib-Kaiser, 2004: 6).

According to the literature contending that globalization may generate crisis and retrenchment in the welfare state, the neo-liberal determinants has altered substance of existing welfare practices once were realized in the Golden Age. Accordingly, intensifying international competition and deregulatory effects of

internationalization of finance and capital brought further deregulation and flexibility in labor markets (Ellison, 2006: 50). Huber and Stephens state that, “Since the 1980s, different dimensions of globalization have weakened both the economic and political bases of generous welfare states (quoted in Brady, 2004: 8). As Pierson states; “The basic outlines of this new conventional wisdom are well known. Globalization undermines the capacity of nation states to control their own affairs and generate acute pressures on the welfare state of advanced industrial societies” (Pierson, 2001: 80).

### **3.1.2 European Integration and Operational Pressures: Single European Market & Economic and Monetary Union**

The European integration which has had both progress and stagnation periods in its history and intensified roughly from 1980s onwards both in economic and political aspects, might be defined as a dynamic part of the recent set of ongoing process via being both an adequate response and contributory mechanism to globalization. Vivien A. Schmidt sees European integration as a regional variant of globalization process (Schmidt, 2001: 1) and Rosamond claims that we may prefer to read European integration as a dynamic component of globalization without necessarily perceiving globalization as *explanans* or as *explanandum* (Rosamond, 2001: 6).

Within this context, two major events in the history of European integration may be seen as the results of being a dynamic part of globalization process. One of them is the establishment of European Single Market via eliminating impediments on the

mobility of goods, services, labor and capital. This could be seen as an operation in line with the chief characteristic of current developments in internationalization of trade, which has been also advocated by GATT and now WTO, as well as accelerated mobility of capital through eliminating controls on capital mobility and production on multinational level.

The second is the formation of Economic and Monetary Union which performs for the complete functioning of internal market and to meet the external challenges through sound economic conditions and together with the introduction of Euro in fifteen member states. Internationalization of financial markets was one of the major reasons which promoted the idea of establishing EMU, in other words, become a European response to this operation of globalization and strengthened its position (Rosamond, 2001).

However, functioning of the European institutions have also influenced the domestic economies and constrict the policy options of the governments, thus generated pressures on the operation of welfare states. Interwoven with external and internal structural pressures, the burden on national welfare states has been, to some extent, raised with these operational challenges emanating from the functioning of Single Market and full implementation of Economic and Monetary Union. Some scholars state that the “restrictive terms of monetary union, represent a far more immediate and pressing constraints on expansive and inclusive welfare provision than globalization *per se*” (Hay, Watson and Wincott, 1999: 6).

In this context, the functioning of single market has directly affected the life of citizens as it foresees the free movement of workers, services, capital which might affect their living and working conditions, the employability in labor markets and create new social risks. Above and beyond, as the mobility of capital has been increased after 1980s, the likelihood to invest to the modestly regulated environments especially with respect to weak social policy has increased. As Geyer indicates, “The fear of member states for social dumping disconcerted them about their social policies and competitiveness” (Geyer, 2000b: 44). Growing internal market increasingly created European level labor whose mobility is increasing and, thus the amount of social risks emanating from this mobility is mounting.

Economic and Monetary Union have affected maneuver of the national member states since it has increased economic interdependence among them and as a consequence left national states limited operational area for the accommodation of labor market and social policies which at the end influences the current arrangement for the beneficiaries of social policy instruments. Accordingly, the room of national member states was gradually limited in designing their own socio-political agenda- as their capacity to use traditional economic policy instruments such as exchange rates, deficit spending, monetary policy has decreased (Jepsen and Pascual, 2005: 237). As Jacobsson denotes “...their autonomy in fiscal policy has been limited by the Growth and Stability Pact. Increased adaptability and flexibility in labor markets have been deemed necessary, as has the need for coordination of fiscal policies” (Jacobsson, 2004: 357).

Overall, diverse approaches on the potential and/or actual consequences of globalization and European integration have, one way or another reflected the attempts to develop empirical assumptions. The literature scrutinizing the changes in international political economy and post industrial transition and its relation *vis a vis* labor market regulations and social policy is highly occupied with the perceived or actual transformations in the welfare state arrangements. At this juncture, as it was suggested above, it is frequently considered that the typical “European Social Model” of post-war period, has happened to be undermined by either the political economy of globalization or European integration, or both (Hay, Watson and Wincott, 1999: 1). By and large, it is suggested that these interwoven processes induced national welfare states to look for manageable solutions and to recast their welfare systems to become compatible with competitive environment and to tackle new inequalities in an age of individualization, globalization and accelerating demographic change (Esping Andersen, 1999, Rhodes, 1996, Taylor-Gooby, 2004 Pierson, 2001).

However, Hay and his colleagues state that “so little attention has been paid to the independent casual and constitutive role of ideas about globalization in the generation of effects attributed to globalization itself” (Hay, Watson and Wincott, 1999: 2)<sup>4</sup>. In their view, discursive construction of globalization-especially the discourse of competitiveness, together with material reality or separately, has had an impact on policy decisions taken about welfare provisions (Hay, Watson and

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<sup>4</sup> They distance their distinction from Mendt’s distinction by indicating that “much of their understanding of globalization rests on the demonstration of the casual significance of discursively constitutive practices (Hay, Watson and Wincott, 1999: 2).



Wincott, 1999: 4).<sup>5</sup> For instance, Jacobsson states that the discourse of the White Paper on *Growth, Competitiveness, and Employment* constitutes one of the good examples of establishing common problem definitions and particular key concepts as well as policy principles as it describes unemployment as a structural problem which can not be merely solved by growth and indicates the lack of flexibility in the labor markets (Jacobsson, 2004: 360). Accordingly the issue of structural reform as well as flexibility has taken in the agenda of European Union as well as national member states as key concepts.

### **3.1.3 New Social Risks in the Era of Post-Industrial Transition**

As it was discussed above, the exogenous and indigenous pressures have profoundly affected the maintaining of traditional discourses of welfare regimes and compelled most of the European countries to enact, to some extent, similar policy reforms culminated with restructuring in social welfare arrangements.

When the Golden Age era come to an end and embedded liberalism gave up its seat to neo-liberal paradigm, policy practices within the existing welfare settlements happened to change. New policy agendas in social and labor market domains have been formed, extensively, within boundaries of new economic paradigm in line with changing world economy. Monetarism highlighting market freedoms with a “strong emphasis on the mobilization of the citizen worker in a more flexible and

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<sup>5</sup> They try to present that “ideas about globalization may exert an independent casual effect on political and economic dynamics irrespective of the material effects to which they refer and that in doing they well serve to summon material effects entirely consistent with the globalization thesis” (Hay, Watson and Wincott, 1999: 4).

competitive labor-market” (Taylor-Gooby, 2004: 13) took the lead and low inflation and currency stability become the priorities of the new economic management. Monetary policy has started to be utilized to hold the inflation at low rates. The rationale behind this was the breakdown of the “virtuous circle”, defined by Martin and Ross, as the linkage between the real wage growth and productivity growth which was established during the Golden Age and later generated the source of inflation. During this era, the labor market institutions –collective bargaining and social benefits- mobilized the mass demand for continued growth and provoke investment while “leaving enough profit to finance investment”. From the mid 1980s onwards, however, the labor market institutions were unable to adjust the real wage downward in accordance with the pressure emanated from the decrease in the productivity growth and the cuts in the national income by “oil price hikes”. Accordingly, real wage rigidity resulted in high rates of inflation, lower investment and slower productivity growth. “The ultimate remedy was to make the labor markets more “flexible” by changing its institutions” (Martin and Ross, 1999: 13).

The new social risks stemming from the post industrial transition are highlighted with a view to understanding the new welfare policy reforms in light of these changes. Three types of changes might be contended as the sources of new social risks. These are; changes in labor markets, changes in household patterns and gender, finally changes in welfare state itself (Aust and Bönker, 2004: 30). The alterations in the form of labor market participation following the technological advancements, demographic changes and new household patterns, determined the

way in which the neo-liberal economic paradigm settled on the new social policy measures to varying degrees. In other words as Rhodes indicates, new market conforming policy mixes have been developed. (Rhodes 1996, p.2)

To be clearer, the advancement in the technology has transformed the traditional work patterns existed in the industrial economies, hence affected the composition of labor market arrangements. “Knowledge based economy” gave rise to more service oriented sectors while the number of employees has declined in the manufacturing sector along with technological advancement. Increased participation of women in the labor market has challenged the male breadwinner model with regard to level of covering unwaged labor costs and care for unwaged work (Taylor-Gooby, 2004: 2).

The national responses to the new social risks and external/internal pressures challenging the traditional welfare arrangements have diverged, to an important extent, with respect to the traditional configurations of interests and institutions previously determined the welfare state formations (Hay 1999, Esping-Andersen, 199. As Taylor-Gooby states, “New social risk reforms are shaped overall by path-dependency, but involve in some contexts new departures.” (Taylor-Gooby, 2004: 13). In this context, a new “welfare architecture” was suggested in the report submitted to the Belgian Presidency of the European Union as a holistic proposal for reforming European social models. Thereby, reforming the welfare states was deemed necessary in the wake of new social risks so as to maintain the original

tenets of European Social Model (Esping-Andersen, Gallie, Hemerijck and Myles, 2001).

Accordingly, different than Keynesian period of aggregated demand management, under the conditions of neo-liberal paradigm and post industrial transition, supply side policies are highlighted to stimulate labor participation through active labor market policies. Taylor-Gooby by referring Pierson and Esping Andersen emphasized the new welfare reforms providing “flexibility of labor market, equal opportunities instead of redistribution of income, social inclusion via integration into paid work and the creation of “social investment state” through supportive social provision instead of compensatory transfer benefits.”(Taylor-Gooby, 2004: 187). Papadopoulos, by referring Esping-Andersen, puts forward that; “The consensus that became hegemonic maintains that welfare states should be transformed into ‘active welfare states’ where state support will primarily focus upon promoting employability in an open market economy” (Papadopoulos, 2005: 4). In other words, the content of social policy and functions attributed to this policy domain has been reformulated with new supply side policies. The initial role of social policy in decommodification has been supplemented and, for certain respect, replaced with a new function of recommodifying the labor in line with changing political economy and post industrial transition. From the 1994 Essen summit, the European Commission has focused on the notion of “active policies” so as to promote the European Employment Strategy (Barbier, 2000:5).

Accordingly, the development of European Union level social policy especially after 1990s seems to carry more workfare oriented characteristics rather than welfare ones. In this respect, Jessop points that, the advancement of welfare as well as workfare strategies at the union level mostly “unified around the concern to create the conditions for an effective single market in the post-Fordist rather than Fordist conditions”. (Jessop, 2005: 45)

### **3.2 EU Response to Welfare State Transformation; Modernizing the European Social Model**

The European Union has been seeking the ways of becoming more competitive in the era of growing international competition together with better employment opportunities. To this end, it endeavors to abstain from the “negative effects of globalization” as well as the new social risks in the wake of external and internal challenges by means of strengthening its social premises.<sup>6</sup> As Taylor-Gooby suggests, in accordance with the new social risks, the EU concentrated more in the area of new deals in social and labor market domains with a willingness to be more influential in the future. However, “its approach to welfare does not fit neatly into the traditional regime framework and its authority is limited” (Taylor-Gooby, 2004: 4). Hereby, a multi-faceted reconciliation happened to be essential. The first aspect of this reconciliation is dealing with the new social risks with new welfare

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<sup>6</sup> “The recently established European Globalization Adjustment Fund (EGF) is an EU-wide response to this challenge. The EGF can spend up to 500 million euros (US\$680 million) annually in EU member states on workers affected by trade-induced layoffs. But sharing the benefits of globalization with the losers is traditionally regarded as a national responsibility.” <http://www.taipetimes.com/News/editorials/archives/2007/05/06/2003359737>

reforms that are consistent with competitiveness and market functioning while adjusting the existing mode of policy instruments covering the old social risks. Secondly, the reconciliation should focus on aligning the diverse national social and labor market policies at the European level in order to constitute common parameters for the growing European internal market. All these efforts have been compiled under the overarching statement of “modernizing the European Social Model”. As Jepsen and Pascual put forward, the process of modernizing the European Social Model was perceived as “the natural response to economic change and globalization”. (Jepsen and Pascual, 2005: 236) Most importantly, ‘social model’ connotation reflected the European approach to deal with challenges arising from social change (Ibid: 237)

The EU Agenda, committing to steadily actualize the abovementioned ambitions, have prioritized employment objectives in different segments. Having experienced persistent Europe wide unemployment, initial measures were, by and large, labor market and employment oriented. Accordingly, Essen Council of 1994 primarily decided to focus on labor market to promote employment and record the employment trends in the EU (Europa, Community Employment Policies).

Subsequent to the Essen Summit, five interwoven objectives were laid down which were formalized in the Amsterdam Treaty under the Title VII and later to become known as European Employment Strategy. These were “promoting employment, reorganizing work, combating social exclusion, mainstreaming gender equality; and consolidation, compliance and enforcement of social legislation” (Adnett and

Hardy, 2005: 7). In the Amsterdam Treaty, it was declared that member states and the Community shall ‘work together’ in developing a coordinated employment strategy. Accordingly, the European Employment Strategy which was designed both to counterbalance the effects of Economic and Monetary Union and as a response to welfare state challenges was launched in Luxembourg Jobs Summit in November 1997. New working method so as to design the employment field has sought the ways of preserving generous welfare state arrangements by reforming them (Trubek and Mosher, 2003:8). This new method foresaw Union level coordination in the definition of common objectives and outcomes while giving responsibility to member states in choosing the detailed content of the actions to member states (Europa, Open Method of Coordination). For being a new form of governance, scholars have debated the functionality of this method from different aspects. Mosher and Trubek indicates that some scholars deemed that EES would be an innovative breakthrough and have the ability to solve the socio-economic problems while others fear that EES would weaken the “efforts to mandate uniform social and employment standards” and “would contribute to the gradual erosion of Europe’s commitment to a distinctive social model” (Trubek and Mosher, 2003:1). Overall, supply-side approach constituted the basis of EES and this strategy complement the other EU and national level policies affecting the realm of employment (Ibid: 8).

The social provision on social dialogue adopted in the Maastricht Treaty was further strengthened with the Amsterdam Treaty in 1997. In order to tackle social exclusion, the Council was enabled to “adopt measures to encourage the exchange

of information and best practice” with qualified majority and co-decision with the European Parliament (Adnett and Hardy, 2005: 5).<sup>7</sup>

An important step with regard to underline the correlation between equity and efficiency was taken in the Lisbon Summit of March 2000 as European Commission declared to become the most competitive and dynamic knowledge-based economy in the world capable of sustainable economic growth with more and better jobs and greater social cohesion.

Most importantly, the EU has promoted the dissemination of the new governance method to other social policy areas in order to mitigate the new social risks and welfare challenges and also give impetus to economic growth and advance competitiveness while providing greater social coherence. Accordingly, in the Lisbon Summit of 2000, a new working method, Open Method of Coordination (OMC) was introduced (European Council, 2000).<sup>8</sup> As stated above, the pioneer of OMC in the late 1990s was the formulation of European Employment Strategy (EES). Henceforth, the OMC has been defined as an instrument of the Lisbon

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<sup>7</sup> As Mosher and Trubek indicates, “the EES anticipates two types of participation by the social partners. The first is participation at the EU level in writing the guidelines, EU reports, and the NAPs. The second is participation in implementing the guidelines on work reorganization. The Commission has attempted to increase participation of both types and in both areas has been only moderately successful.” (Trubek and Mosher, 2003:25).

<sup>8</sup> The key elements of OMC are defined as follows; a)fixing guidelines and timetables for achieving short, medium and long-term goals, b)establishing quantitative and qualitative indicators and benchmarks, tailored to the needs of Member States and sectors involved, as a means of comparing best practices, c) translating European guidelines into national and regional policies, by setting specific measures and targets, d)Periodic monitoring of the progress achieved in order to put in place mutual learning processes between Member States. (EC.Europa, Open Method of Coordination)



strategy which involves soft law measures and takes places in areas which fall within the competence of the Member States, such as employment, social protection, and social inclusion (Europa, Open Method of Coordination). Although soft policy coordination had already developed in employment policy-European Employment Strategy-, this time it was extended to the aforementioned sensitive areas. The OMC, in essence is an intergovernmental cooperation. Yet, it encompasses supranational elements as well as stipulates broader participation of social partners and subnational actors (Jacobsson, 2004: 357).

The crucial term is policy convergence instead of harmonization. Rather than convergence of means, this implies the convergence of objectives, performance and to a degree the policy itself. According to Jacobsson such elements comprise a systematic governance mechanism which could help to change member state practices and contribute to the integration process by a different type of regulation than hard law (Ibid: 356). Furthermore, Jacobsson regards the OMC as a methodology including a variety of “discursive regulatory mechanisms” that are influential in member states’ policy making. He defined them as;

joint language use (key concepts and discourse), establishment of common classifications and operationalizations, building of a common knowledge base, the strategic use of comparisons and evaluations, systematic editing and diffusion of knowledge and evaluation results, and all of the above combined with social pressure -peer pressure and time pressure-(Ibid: 360).

At this point, he suggests that the existence of a common vocabulary and a cognitive framework is useful for interpreting the challenges and for delivering policy solutions more delicately (Ibid. 360). This “new paradigm” of European Integration was constructed with the principle that the EU can “provide the

orientation to” arrange economic, employment and social policy such that each could be supportive rather than detrimental to the other (Hermans, 2005: 6)

The perception change of the European Commission stipulated the initiatives in the European social sphere. In the Rome Treaty, the social policy was envisaged as the “by product of economic policy” since the definition and perform of it were left in the hands of member states, although it aimed at unification of the economic policies. Yet, after the European Council of March 2000, so as to say Lisbon Summit, the perception of the Commission regarding social policy transformed and social protection has been acknowledged as a “productive factor”.<sup>9</sup> (O’Connor, 2005: Hermans, 2005).

In response to the call of Lisbon Strategy, the Commission set out a Social Agenda (2000-2005) encompassing measures to reach the targets of the Lisbon Summit. To this end, the Commission Communication on social policy agenda constituted the basis of the agreement reached by Heads of State and Government in Nice Summit. In the Summit, the role of the Agenda in terms of “strengthening and modernization” of the European Social Model has been highlighted (Hermans, 2005: 9).

In sum, a discourse on employment and social welfare was developed in Europe throughout the 1990s, which rose above the concepts like “employability,

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<sup>9</sup> The initial contextualization of the social policy as “productive factor” was in the conference organized during the Presidency of the Netherlands of the European Union in 1997. For more information, please see, (Hermans, 2005)

adaptability, flexibility, activation, lifelong learning, social inclusion, active welfare” (Jacobsson, 2004:360).

The emphasis on social cohesion and European discourse built on European Social Model was later strengthened with the Commission statement in the Draft Constitution of 2003 to work for “Social Market Economy”. Social Market Economy stands as a socio-economic theory aiming to balance social justice and economic efficiency with a view that competitiveness does not necessarily challenge the social welfare.

Commission’s statement to work for Social Market Economy has served to reproduce the efforts to create a triangle among economics, employment and social policy and has been an attempt to legitimize the social and labor market reforms. There is an interconnection between European economy and European “social dimension”. In this regard, at least to a certain extent, the notion of ESM is considered carrying similarities with the German concept of social market economy. (Barbier, 2006: 122) which will be explored in the following chapter.

## CHAPTER IV

### SOCIAL MARKET ECONOMY IN THEORY AND PRACTICE

There is hardly any term used to mean so many different things in public discussions as that of the Social Market Economy is believed by many today to be the model *per se* for an economic and social order. It is therefore not surprising that the term is widely misused a “Trojan Horse”, a concealing what are often decidedly interventionist ideas which actually go against the grain of the concept.

(Tietmeyer quoted by Nicholls, 2000:4)

Being one of the first and leading Member States of the European Union, Germany has influenced the process of European integration in many aspects to varying degrees. The economic structuring of the European Union such as establishing European Central Bank similar to German Bundesbank constitutes one of the examples of this interaction. Recently, its Social Market Economy model which was introduced in 1948 has inspired the European policy makers and European social actors as a constituting principle laid out in the European Union Draft Constitution of 2003.

Social Market Economy mainly depicts a type of market economy which aims to achieve market effectiveness, competitiveness and social justice through combining market freedom with social equity within a constitutional framework. (Koslowski, 1998) The terminology of Social Market Economy appeared in the world history following the attempts of constructing theoretical and politically practical solutions to the socio-economic deterioration in German political

economy, which have been intensified after WWII. Despite the theory of Social Market Economy was coined after 1946 by German intellectual Alfred Müller-Armack, its intellectual roots, dates back to 1930s, when the economic failures of the interwar period churned the German economy profoundly.

The theory of Social Market Economy came into practice in West Germany in 1948 with the policies of Ludwig Erhard, Economic Minister of CDU, subsequent to the attempts of reconstructing the German economy following the devastating Second World War. It came to the fore as a feasible option for the recovery of the German economy as it pledged to satisfy the fundamental and legal grounds for the functioning of market economy on the one hand and including socially balanced aspects on the other. It was a product of the revisited liberal thought in Germany subsequent to the socio-economic deterioration in 1930s.

The concept of Social Market Economy is mostly regarded as the driving force behind the German miracle of 1950s and 1960s. Following the introduction of Social Market Economy as the economic program of Germany in 1948, a major export oriented economic boost happened and carried Germany to the list of the most competitive economy together with US and Japan. Consequently, German capitalism stood out with its both traditional social institutions and Social Market Economy among other capitalist form of economies in Europe. As Streeck states;

in the roughly four decades between the end of World War II and German unification, West German society gave rise to a distinctive kind of capitalist economy, governed by nationally specific social institutions that made for high international competitiveness at high wages and, at the same time, low inequality of incomes and living standards (Streeck, 1997: 33).

Apart from the German experience of Social Market Economy, it is argued that there have been other countries, principally Austria, practicing the concept in various ways (EC.Europa, The European Social Fund in Austria). However, the implementation of the theory has differed as the theory came into practice within the different traditional national frameworks. In this chapter, the German experience of Social Market Economy is scrutinized since the initiators of the concept were mostly German intellectuals influenced by the German political economy and developed the concept inseparably from the German historical experience.

Throughout this chapter, the theory of Social Market Economy, its intellectual roots and foundations as well as its evolution through history is examined. As the economic and political conjuncture of 1950s has remarkably changed, the theory has been relatively loaded with different meanings by different scholars. First, it examines the rationale behind introducing the theory as a new socio-economic order for the West Germany after the Second World War. Secondly, the Ordoliberal roots and works of its founding fathers are investigated. Finally, the adjective of “social” in the Social Market Economy and the connotations loaded to the concept is tried to be scrutinized. It is for the next chapter, which will ground on the framework drawn here, to evaluate the intentions of the different actors at the European Union by referring “Social Market Economy” in their discourses.

#### **4.1 Examination of Social Market Economy from a Historical Perspective**

The defeat of Germany in World War II resulted in economic destruction and political uncertainty in the country. The country was occupied by the Allied Forces and its economy collapsed. Germany's defeat in the war brought about devastating result for both economy and social life, especially in terms of capacity lost of infrastructure, housing and manufacture (Rösner, Jürgen and Werner,1996: 21). The issue of restructuring German economy was taken to the immediate agenda of politicians and economists who supported various political thoughts. Various programs were suggested so as to reconstruct the economy. However, the international economical and political conjuncture of the time as well as the influence of Allied Forces became the determining factors in choosing the viable economic alternative for Germany.

After Germany was defeated in the Second World War, she was divided into occupational zones. It was occupied by Western Allies. The power of the Western allies in inspiring and shaping the future of Germany was of a great importance (Smith, 1994: 5). Their attempts to integrate Germany into international economy and the infusion of capital through international aid paved the way for the selection of the market economy. United States considered the resurgence of German economy essential for the stabilization of the region and for international economic ties. The prime importance to the Allied Powers was relocating German economy to integrate it to international economy. In due course, the U.S. encouraged German economic recovery within the framework of European recovery. German

economic rehabilitation was seen inevitable for a prompt and successful restoration of the European economies (Smith, 1994: 8). International aid which was financed through Marshall Plan provided the economic means for the European economic recovery. Marshall Plan stipulated the European aided countries for further economic corporation and open up their markets. Therefore, the attempts of Western Allies to embed Germany in international economic environment and infusion of capital through Marshall Plan within the framework of European recovery motivated with the idea of securing political stability strengthened the bases for establishing a market economy framework for Germany.

The option of *laissez-faire* capitalism was refused by a line of scholars, namely Ordoliberals, such as Walter Eucken, Wilhem Röpke, Alexander Rüstow as it was blamed for social and economic distress in 1930s and 1940s. According to them, the premise of *laissez-faire* capitalism lost its credibility after the economic crisis induced by Great Depression. They deemed that the history of *laissez-faire* capitalism proved that free market lacking legal framework and social balance has the tendency to generate chaotic results in social sphere. In their view, the historical experience showed that the free market economy system was vulnerable to the manipulation of dominant economic forces which in the end produces the tendency towards cartelization tendency and distorts competition.

Within this context, a novel version of the market economy was deemed necessary so as to fill the gap of the legitimacy of liberal premise. The inquiry into liberal theory was reflected in Germany with the development of Ordoliberal idea which



is defined by some scholars as the German type of neo-liberalism and constituted the basis of Social Market Economy (Giersch, Paque, Schieding, 1992; Sally, 1998). Leading figures of Ordoliberalism, namely the Freiburg circle, rejected the Adam Smith's 'invisible hand' which envisaged a harmony among different economic interests. Instead, they proposed an economic system with a constitution provided by the state that guarantees the well functioning of the free markets by impeding the dominance of vested interests which has the tendency to distort the competition (Goldschmidt, 2004: 9). Consequently, this market economy would not function on the basis of laissez faire capitalism but on the contrary it would be based on "order". In other words, the spontaneous actions of the market should not constitute the basis of the market order. Rather, the order itself needs to be established through a "consistent order-based policy (ordnungspolitik) of the state" (Peacock and Willgerodt 1989, 242). Accordingly, state or government intervention is to be seen as the producer of the market (Peacock and Willgerodt 1989, 242). This is not to say that there should be a central planning or state interventionism, but there should be an economic framework and general principles of economic policy, to which politicians must adhere (Goldschmidt, 2004a: 4).

Besides, balancing the legacy of National Socialist collectivist organizations for planned economy was substantial for the reorganization of the socio-economic order. Overall, having relied on the scientific and intellectual support of Ordoliberals, who contributed to the works of the independent council established by Economic Administration in late 1948, Ludwig Erhard strengthened his stance

for the implementation of Social Market Economy program (Lachmann and Rösner, 1995: 22).

#### **4.2 Intellectual Roots and Institutional Foundations of Social Market Economy**

The theory of Social Market Economy has a distinctive character with its eclectic structure and configuration which enabled diverse interpretations in light of changing economic and political environment. Although it has constant features such as market freedom and social justice, the reading of the concept differs from one intellectual to another. As a consequence, there exists more than one interpretation of Social Market Economy.

Alfred Müller- Armack, who was the head of the Central Policy Unit at the Federal Economic Ministry, coined the term and the theory came into practice with the economic program of Ludwig Erhard in 1948. Armack was not the only one behind the creation of Social Market Economy theory. The intellectual roots of the theory have been mostly shaped with the contributions of Ordoliberal intellectuals such as Franz Böhm, Walter Eucken and Alexander Rüstow and Wilhem Röpke (Vanberg, 2004).

Social Market Economy theory encompasses various philosophical backgrounds which date back to Christian social teaching (Lachmann and Rösner, 1995: 26). Humanist principles constituted one of the bases of the Social Market Economy.

The influence of the Christian social values was tangible in the expression of the social responsibility and solidarity. However, the most important contribution was made by Ordoliberal theorists.

#### **4.2.1 Ordoliberalism and its Contribution to Conceptualizing Social Market Economy**

The seeds of Ordoliberal theory were sowed in the Weimar Republic following the economic downturn after extensive inflation and Great Depression and developed during the era of Nazi domination. At the time of economic deterioration in mid 1920, Germany was remarkably characterized with its highly cartelized economy. The dominance of vested interest on the state and the subsequent significant state intervention determined the economic conjuncture of thirties and forties in Germany (Nicholls, 2000). German Model stood as unique example of industrialization among Western European Countries.

Liberal theory flourished in Germany in the early 19th century which was a bit later than Anglo-Saxon liberalism. Besides, German type of liberalism differentiated from Anglo-Saxon type along with the form of industrialization which was determined by the state paternalism and corporatist institutions united the political economy. In spite of the tardy industrialization process, in a short period of time, Germany became of the leading industrial nation in the European continent. Although the expectation of German liberals that the unification would abolish restrictions on trade and industry was satisfied to some extent, the liberal

movement weakened together with economic failure of 1880s and incorporation of corporatist elements into political economy by Bismarck. According to Smith “the break with Liberalism started in Germany during the last quarter of the 19th Century; since then an economic system which is aptly described as interventionism gradually evolved in Germany” (Smith, 1994: 48).

Nicholls interprets this as “the protectionist measures and the German capitalism’s pursuit of government interventionism were settled as it had to fight against settled competitiveness of Anglo Saxon countries” (Nicholls, 2000: 16). Consequently, there was a trend of cartelization in the 1920’s Germany and Germany was called to be “the land of cartels.” The growth of cartels seemed essential at the time of economic recession in 1870s and supported through legal framework, however by mid 1930s they were blamed for hampering the free competition (Ibid: 19).

Ordoliberal theory was extensively built upon the critiques of state interventionism raised subsequent to two significant economic failures of Weimar Republic. Nicholls states these economic failures as “the rampant inflation which destroyed Germany’s currency in the period between 1918-23 and the second was the Great Depression, which brought with it widespread economic ruin, and the victory for Adolf Hitler” (Ibid: 13). Economic adversity of interwar period was doubled with the political crises and Nazi domination. The distress of German neo-liberals was intensified as the human freedom and freedom of economy were restricted. In addition to national experience of economic failures, the turbulence of Great Depression in the world economy affecting the all political economies had

seemingly discredited the prevailing liberal orthodoxy. The deepening social malaise served only to increase the magnetism of fascism and communism. According to the Nicholls, there was a wide belief that anarchy of the market and capitalism were in charge for the depression (Nicholls, 2000: 16). Within this context, some line of liberal intellectuals revisited the elements of liberal thought and endeavored to find a way out between laissez faire and totalitarianism (Sally, 1998:106).

The critique of Freiburg School about state interventionism in the Weimar period and its contribution to market economy mentality which was different from laissez faire policies founded the bases of Ordoliberalism and later contributed to the conceptualization of Social Market Economy. Regarding laissez faire policies, Ordoliberals deemed that if market economy left its own, the “invisible hand” of market will not necessarily assure the well functioning of market mechanism and the market forces will incline to create power concentration in the end which distorts competition. According to Ordoliberal theory, market mechanism should be structured in a legal framework and work in line with constitutional order.

Ordoliberals contend that laissez-faire liberalism did not wholly comprehend the decisive positive role that government has to play in creating and securing a proper framework of rules and institutions that allows market competition to work effectively. For Ordo-liberals, market order signifies a constitutional order. That is to say, the actors depend on legal-institutional frameworks for shaping their action, and this would be discussed as a constitutional issue (Vanberg, 2004: 5). The

purpose of Ordo-liberal theory was to establish the legal institutional conditions in which the actors seek their own interest can as well augment the common interest (Vanberg, 2004: 8).

#### **4.2.2 The Contextualization of Social Market Economy by Alfred Müller-Armack**

As it was stated above, the conceptualization of the Social Market Economy was not limited to the principles drawn by Freiburg circle of Ordoliberal thought. As a comprehensive terminology, the concept was reinterpreted and strengthening with the practical economy policies of Ludwig Erhard and materialized with contributions of its founding father, Müller Armack (Tezuka, 2001: 203).

Müller Armack systematically reinterpreted the Ordoliberal approach through analyzing and synthesizing the ideas suggested by the Ordoliberals with his own contributions. Even though Müller Armack had generally been associated with ordo-liberals, he cannot be counted as a member of Freiburg School. He was a professor of economics in Cologne and according to Michael Wohlgemuth, Cologne mode of Ordoliberal thought distinguished from Freiburg circle along with its objective to merge individual freedom in markets with social justice and balance through government intervention (Labrousse and Weisz 2001: 5). While Ordoliberals' view is more market oriented with little place given to state interventionism, Armack, on the contrary, developed rather more eclectic version which was open to state interventionism (Lehmbruch, 2005: 84). At a time when

the proponents of “Christian Socialism” strongly supported the goal of full employment- opposed by Ordoliberal-, namely within the CDU during Adenauer presidency, Armack’s eclecticism proved evidently superior to the ‘doctrinal rigidity’ of the Ordoliberal views for the unity of party and political integration. Thus, this eclecticism clearly managed to combine Ordoliberal concept for institutional order of market and social policy emanated from Social Catholic tradition (Lehmbruch, 2005: 84).

Müller-Armack, indicated that market economy stands as an economically most efficient order, however, it does not necessarily have an inherent ethical character. Instead, it should be seen as efficient technical instrument which can be used by society to produce wealth. Additionally, it must be supplemented with the methodology of generating a particular social policy. These policies should be embedded in order to give the market order the ethical quality (Vanberg, 2004: 2).

According to Armack,

“the co-ordinated functions of the Social Market Economy do not conform exclusively to the mechanical rules of competition. Its principles and organization relate to State and society, both of which impress their notion of value and responsibilities on the whole system of the Social Market Economy”(Armack, 1998: 258).

Armack named his theory as an “irenical order” as it pledges to integrate the crucial forces of society into a mode of co-operation. To be more clear; individual freedom, economic and social security and growth are usually regarded as conflicting objectives trying to succeed at the expense of the other. Yet, Social Market Economy claims to be an “irenical order, a strategical idea within the conflict of different objective-situations... Social Market Economy is a social

solution in which all objectives are brought into a workable, realistic harmony” (Armack, 1998: 261). The Social Market Economy tries to reconcile the conflicting abovementioned objectives through currency stability, growth, full employment and also equilibrium in the balance of payments (op.cit).

Armack regards Social Market Economy as the ideological concept which is knitted with the co-ordination of the spheres of life represented by market, the state and the social groups (Armack, 1998: 258). Thus, the equilibrative characteristic of Social Market Economy is at the high importance for both the conditions of the ‘working of the market economy’ and for the ‘relationship between the economic order and other orders of the society’. The concept of Social Market Economy includes the idea that the economic system pursues objectives of social security and social equilibration in the sense of reducing extreme income differentials (Koslowski, 1998: 84). The Social Market Economy first and foremost equilibrates free initiative of individuals and social advancement measured also in terms of social security, with regard to competitive aspect of economy. This socio-economic progress is calculated with the performance and efficiency of the market economy. (Ibid: 82). In addition to this, Armack emphasized the importance of granting adjustment subsidies which secure the sectors such as textile, agriculture and mining- exposed to pressure of economic forces or under the pressure of competing products to capable them to adjust to the competitive situation (op.cit).

The notion of “strong state” was underlined in the conceptualization of the Social Market Economy. It was a response to the attitudes of weak governments in



Weimar Republic which had become increasingly open to the ‘rent-seeking of the private sector interest groups’ (Carlin, 1996: 483). According to the theory; the state should be strong in the sense that it distances itself from the pressures and appeals of any interest groups. The strong state statement is not defined in terms of intervening in the functioning of market economy but as a “guarantor” securing and maintaining the appropriate legal and institutional framework within which the market economy would work efficiently. The state should have an active responsibility in pursuing to correct the inequalities that cannot be overcome through natural course of market mechanism and competition per se (Schlecht, 1998: 280). Therefore, state is supposed to follow two different major roles; first it should create and sustain “the order”. Secondly it should define the policies where it can intervene in the cases where markets are incapable of balancing the outcomes for the social justice.

The adjective “social” refers to several meanings in Social Market Economy. Public care and socially responsible state intervention lie at the heart of the adjective “social”. To be more specific, social adjective refers to social security. The role of the state is defined with the responsibility of assisting weaker individuals of the society who are not or partially able to participate in the market for reasons of health, age, lacking source of income, etc. Müller-Armack incorporated the necessity of socio-political equilibrium in his study of Social Market Economy. The statements made by Armack for the socio-political equilibrium are designed to provide the necessary conditions for improved participation in employment, humanized living and working conditions. These are

provided with better education system facilitating the access to qualified employment, assisting the medium-sized firms to flourish, improving the process of enterprise through decentralization of decision making and humanization of working conditions, etc (Nörr, 2000: 229).

Müller-Armack constructed a kind of social policy providing an integration formula intervening constructively in order to lessen the tension in the society as much as possible on the basis of joint action and embrace the agents and actors of the society as far as it manages (Armack, 1998: 264). However, this integration formula does not mean changing the statuses of the strata of the society, as safeguarding the actual group which the individual belongs is highlighted (Ibid: 267).

According to Armack's depiction of the features of social policy in the Social Market Economy; further development of social security and the equilibration of income differences in a manner compatible with market economy is a crucial factor. Among these features, the constitution of a social order in which minimum wages are emphasized together with a significant value given to the worker (Koslowski, 1998: 89).

According to Lehbruch "Müller Armack considered the redistributive welfare state as justified under the proviso that this redistribution did not distort the functioning of markets and he explicitly defended government regulation of utilities transport, agriculture and credit system" (Lehbruch, 2005: 84). Social

market economists suggested a contribution based financing of the social security systems. According to their view, progressive tax system and subsidies, compensation payments should be utilized as means of redistribution policy correcting primary distribution (Leipold, 2001: 340).

#### **4.2.3 Critiques on the “Social” Adjective of Social Market Economy**

The Social Market Economy, theorizing economy and transcending it, has been debated starting from its early stages of implementation up to the present. Specifically, the social component of the theory has been a main source of debate and is a continuous matter of dispute among scholars in the evaluation of the Social Market Economy.

Aforementioned, the role of the state in realizing social tasks was emphasized in the conceptualization of the Social Market Economy theory. According to Lehbruch, “state intervention in conformity with market became magic formula for this accommodation of the ordo-liberal doctrine to social policy and helped to reconcile it with the heritage of state led social reform” (Lehbruch, 2005: 85). The critics of Social Market Economy argue that it would be impossible to guess where the interfering state intervention starts at which point as state intervention might transcend the threshold at which disturbance to the functioning of the market begins (Leipold, 2001: 341).

The role and the position of the social policy have been widely discussed within both the Freiburg School and Cologne Circle emphasizing the necessity of an economic order as the constitution for the market game. However, they had diverse notions of social policy as a fundamental principle of a functioning market system (Goldschmidt, 2004b: 66). Boyer notes that “Social Market Economy does not contain commonly accepted measures of social justice”. (quoted in Goldschmidt, 2004b: 65). Nonetheless, Müller Armack endeavored to clarify the basic features of the social policy in the Social Market Economy as it is stated above.

The constitution of the Basis Law for the Federal Republic of Germany of 1949 declares in the Article 20 that The Federal Republic of Germany is a democratic and social Federal state.<sup>10</sup> Hereby, the social state emphasis is regarded as one of the irreversible fundamental basis on which the German society organized. In the constitution of the Federal Republic of Germany, there are several provisions regarding employment and labor related issues. The proponents of Social Market Economy argue that integrating several provisions on employment and labor indicates that the labor market order was designed in accordance with the economic, social and constitutional order (Nativel, 2004: 66). Nativel, through referring Stein, says that these provisions are entirely applicable to the notion of social equilibrium inherent in the Social Market Economy and labor market policies have their place within Social Market Economy mechanism together with macroeconomic policy and the system of industrial relations as they are in conformity with the principles foreseen in the Social Market Economy theory. She

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<sup>10</sup> For detailed information on Basic Law for the Federal Republic of Germany, see; <http://www.psr.keele.ac.uk/docs/german.htm>

continues by saying “theoretically there is a genuine complementarity between order policy and social policy” (quoted in Nativel, 2004: 66).

However, some critics on Social Market Economy claim that;

“welfare within the tradition of economic constitutionalism was not compensatory but was perceived largely as an instrument of economic reform to create a more competitive and entrepreneurial forms of conduct within social institutions. Accordingly, the economy and society only serve to reinforce the fundamentals of the economic order of society; hence social intervention can be justified if it has a substantial impact on the reproduction of economic order” (Peacock and Willgerodt 1989, 244).

#### **4.3 “Social” Market Economy Theory in German Practice of Welfare State**

The articulation of the adjective “social” in the Social Market Economy have been developed and evolved within the dynamism of German industrial relations and traditional welfare system whose roots can be traced back to Bismarck’s social legislation of 1881. Although the Social Market Economy has been developed as a socio-economic theory having general assumptions and implications, the influence of existing socioeconomic structures had an impact on its implementation which eventually created a perception that it is a German model. As Streeck indicates;

since there have been a strong and complex compromise between liberal capitalism, as introduced after the Second World War, and two different countervailing forces, social democracy and Christian democracy, liberalism and socialism, and of course between capital and labor, those who wanted to turn the new Germany into a liberal market economy had to accept the revival of a variety of traditionalist status protections—for farmers, civil servants, *Mittelstand* and the like—as well as an extensive welfare state and established labor unions (Streeck, 1997: 238).

Manow stresses that; German welfare state has been characterized with its federalist, autonomous and less state dependent features. Indeed, there was a

compromise between the central legislative powers and local Lander governments in public administration, especially in terms of delegation of responsibility to Lander. Social insurance has risen above existing collective self help and self demonstration mechanisms. Accordingly, these structures were brought about the division of financial burden and administration among workers, employers and the state (Manow, 2005: 111). In spite of its federal structure, social policy legislation is realized at the national level (Leibfried and Herbert, 2003: 201).

Overall, German type of capitalism differentiated from the other European political economies and the mode of Social Market Economy gained a distinctive character along with distinguishing set of socioeconomic institutions. Especially after mid 1960s and early 1970s, German Social Market Economy was associated with the extended rights for labor representation and social partnership.

Within the typologies of welfare state, German welfare state has been typified as conservative welfare state (Esping-Andersen, 1990) along with its maintenance of status differentials through earnings related transfer approach and references to the principles of Christian social teaching, subsidiarity and male breadwinner model as well as rejection of class struggles via applying corporatist conflict resolution. It has been structuralized and administrated in line with the subsidiarity and decentralization principles.

Keynesian employment policy and establishment of corporatist arrangements for setting wages were disregarded in the Ordoliberal elucidation of Eucken as he

considered that these institutions would not only have side effects and but also would give rise to monopolistic market structures. However, as Witt indicates there did develop a corporatist order of the sort Eucken opposed as a result of “postwar Germany’s legal sanctioning of the freedom to form coalitions in the Basic Law and the right to autonomy in centralized wage determinations by trade unions and employer associations.” In line with abovementioned arguments, Witt argues that:

Indeed, this special arrangement appears to have contributed greatly to the willingness of the German trade unions to make their peace with the German economic constitution, even though their socialist position initially led them to oppose the Social Market Economy. The arrangement remains in operation today, and, under the name *social partnership* it has become part of the theory and practice of the contemporary Social Market Economy (Witt, 2002: 317).

There has been a strong linkage and consultation among trade unions, employers’ associations and government leading to policy advice. In due course, social partnership “between labor and employers’ association and the state willing to mediate the diverse economic interests” is condemned to be the major pillar of the industrial relations and the interest representation (Berger and Compston, 2002: 125).

The economic governance in industrial system of Germany has extensively relied on the participation of employee representatives in decision-making process at the board level and granting the rights to the employees for information and consultation at the establishment level. By this means, labor market actors are classified as social partners with an idea to reach common decisions on the issues concerning the corporate governance. This has been highlighted with the *co-determination* concept resting on the notion that the suppliers of equity capital and

the suppliers of labor run the firm cooperatively (Gorton and Schmid, 2004: 864). Most importantly, *collective bargaining* between trade unions which are organized at the industrial level in order to negotiate sectoral agreements and employers' associations at the industrial level has been at the heart of German industrial relations.

Social Market Economy has been engendered within the traditional framework of the German welfare and social work system and evolved in accordance with the alterations in the German welfare system. Although the main principles of the German mode of welfare system stayed intact, the configurations of the institutions of welfare state and social work have slightly changed in line with the changing economic and political conjuncture which let us draw a multi-phased picture of implementing Social Market Economy.

The first phase of Social Market Economy (1948-1963) was the constitution of the market economy in Germany. In this early stage of resurgence of the German economy and implementation of Social Market Economy, the emphasis was made more on the "market" rather than "social" seeing that market-making was the initial goal of the policy makers and the economic applications of Ludwig Erhard's ideas were more influential with the premises of Ordoliberal theory. However, Basic Law of 1949 puts strong emphasis on the administration and regulation of social policy (Ginsburg, 1992: 66). Social Market Economy program had not implemented the Keynesian macroeconomic design in its practices in its early implementation. Monetary stability has established the basis of the Social Market



Economy. However, the second phase of Social Market Economy (1966-1979) starts with an economic recession in 1966 which led the resignation of Erhard and transition to Keynesian aggregate demand approach and continued until early 1990s.

When the Erhard's tenure came to an end following the economic downturn, the first episode of the West German Social Market Economy closed and a new period designed with the policies amalgamating the "Freiburg imperative" to "Keynesian demand management began (Wünsche, H.F. & Stiftung, L.E. & Ludwig, Derek R., 1982). Beginning from the mid 1960s, Germany started to be termed as "socially controlled welfare capitalism". (Sengenberger 1984). The emphasis was given to neo-corporatist features and generous welfare provisions (Lange, J. R. Shackleton, 1998: 2). The government intervention in social field increased and during this period, West Germany experienced managed growth. Precisely this point constitutes the ambiguity of the Social Market Economy therefore varied interpretations of the concept. Accordingly various arguments are developed around the original concept of Social Market Economy and differentiated with regard to its implementations.

The political figure of the time was Schiller, The Minister of Economic Affairs from SPD, who profoundly influenced the economic policy making. He was a liberal minded intellectual supporting the Ordoliberal approach to economic constitutionalism. However, he deemed steering mechanisms and a variety of economic tools, including state regulation were necessary so as to sustain the

economic achievements and economic upturn. Accordingly, Schiller suggested a kind of amalgam of planning and competition, both of which complements each other (Nicholls, 2000: 306-307). His concept for this new economic design was 'Globalsteuerung' which means global steering. This term connotes a process in which the government establishes merely a framework so as to promote non-inflationary growth. According to him, competition and freedom in the market ought to be legally protected as much as possible, however state regulation has to be applied where the market is unbalanced. Besides, national economic budget should be generated to support the progresses in the economically and socially advantageous areas (Ibid: 307). This approach can be distinguished from neo-liberalism as it foresees state interference where it is necessary, while neo-liberalism only consents to state activity which protects the framework in which market could function (op.cit).

Welfare state provisions were extended and labor interest representation such as co-determination at work place was enhanced during the Grand Coalition tenure. By the mid 1960s, SDP put much emphasis on macro economic planning through national budget, social equitable taxation and establishment of co-determination in industry. According to Nicholls; "In this respect the objectives of SDP began to converge with those of the more socially concerned adherents of Social Market Economy" (Ibid: 309).

Along with the changes in the practicing Social Market Economy, scholars debated the flexibility of the Social Market Economy concept in terms of its social policy

implications. As it was elaborated above, some of the scholars states that more welfare state oriented policies are not foreseen in the theory and growing tendency to implement more comprehensive welfare policies transcends beyond the theory. On the other hand, another line of scholars claims that Social Market Economy was developed in conformity with the changing economic and political environment, thus, as long as the provisions do not threaten the functioning of market economy and competitiveness, the appropriate social policy development would be in conformity with the theory itself.

In the wake of international adjustment pressures in the 1970s, Germany succeeded to embed elements in her system and showed a significant growth together with its stable and industrially adaptable economy. Germany's successful economic adjustability was due to the establishment of an independent central bank that focuses on price stability, an "enabling" state that supports firms and banks, and neo-corporatist industrial relations (Schmidt, 2002b: 166).

From the early 1990s onwards, Social Market Economy started to be knitted with more neo-liberal features along with the transformative pressures emanating from international competitiveness, European economic integration and economic costs of unification respectively. Accordingly, the third period of Social Market Economy gained more neo-liberal characteristic and welfare state transformation which brought neo-liberal adjustments to "social" adjective of economy. The increased incorporation of market elements to state led capitalism of Germany was realized by the CDU-led government in the early 1990s (Ibid: 165).

The external and internal pressures challenging the existing practicing of Social Market Economy are interpreted by the Streeck as the crisis of the German “Social Market Economy”. Streeck connotes that both the internal and the external forces can be considered as the crisis of the existing exercise of the German social market economy. According to him, the lasting success of social market economy looks dubious. Furthermore, the chance of survival of the model depends on its ability to overcome the challenges through the enlargement to the newly integrated East Germany as well as on its harmonization to European integration process, an important aspect of the latter being the EMU (Streeck, 1998: 2).

## **CHAPTER IV**

### **A EUROPEAN SOCIAL MARKET ECONOMY?**

Few of Germany's bankers and politicians have dared to brave the tide and come out in support of the social market economy, the precepts of which have been betrayed in its country of inception and whose concepts have been forgotten in the rest of the world. That is unfortunate. In times of financial crisis, this approach could become one of the Germany's most successful exports (Gerke, Financial Times, 2008:11).

European Union has not developed a common European social sphere; still it aspires to constitute a common European vision in response to external and internal pressures that challenging the existing welfare state structures and policies. In spite of the diverse responses of national states given to aforementioned constrains, the overall economic and social objective, designated by the Commission in the Lisbon Summit, induced the EU to adopt new roles in the social field and to assist the modernization of the "European Social Model". This might be considered as one of the ways of seizing the "window of opportunity" for the Commission to step in designing the European social dimension while strengthening its legitimacy as a European institution.

The attempt to modernize the European social model has emanated from the need to recast the traditional European welfare systems in compliance with the recent changes in the world economy and adjust its institutions in accordance to the post industrial transition while relieving the apprehensions for the lack of a "Social

Europe". This attempt has become more evident with the EU declaration stipulating to become the most competitive knowledge based economy with greater social cohesion as it was declared in the Lisbon summit. The political discourse of the Lisbon Strategy, associating "greater social cohesion" and "increased competitiveness", has further strengthened with the incorporation of "Social Market Economy" notion in the draft EU Treaty and later in Lisbon Treaty of 2007.

As it was stated in the fourth chapter, the proponents of Social Market Economy famed the model with its combination of market efficiency with social justice, therefore many scholars and politicians related the Social Market Economy concept with the German miracle of 1950s and early 1960s. Though Social Market Economy concept was referred by different scholars in various associations, the normative connotations of the concept have mainly revolved around two notions, namely "social justice" and "market efficiency". German variant of Social Market Economy concept was developed as a socio-economic order in response to the necessity to reconstruct the collapsed German economy after the devastating Second World War. Market formation was the initial aim of Social Market Economy. The proponents of Social Market Economy alleged that its institutions were designed to combine competitiveness with social balance. In this manner, the equilibration feature of the theory was envisaged to balance the consequences of being a competitive economy through equilibrating between free individual initiatives and social advancements.

This chapter mainly scrutinizes the grounds of introducing the Social Market Economy notion in the EU documents following the efforts to attain the Lisbon goals. Accordingly, it investigates the anticipation of social partners and the Commission in espousing the concept in their discussions revolving around European social model and Internal Market. The following question whether the notion of Social Market Economy and new policy tool flexicurity could be mutually reinforcing in strengthening the political discourse of European Union in promoting common responses given to economic and social change by means of Open Method of Coordination.

### **5.1 Assessing the European Social Model from the Perspective of “Social Market Economy”**

With regard to assessing Social Market Economy Theory at the EU level, an examination is made between exploring the feasibility of applying the theory with its original tenets and adopting the normative associations of the concept in EU political discourses. Conventional wisdom associated the concept of Social Market Economy with traditional socio-economic institutions generating generous welfare benefits and encompassing broad social dialogue mechanisms (Glasman 1997, Iversen, Soskice and Pontusson, 2000). Most importantly, the concept is regarded as a European model framing distinct welfare states of the post war era. As Hemerijck indicates Social Europe is built upon unique harmony of normative, cognitive and institutional characteristics, hereby “European social market economies do share a number of common characteristics” (quoted in Seters, 2006:

111). However, the original tenets of Social Market Economy did not *per se* encompass the elements of corporatist market economy. As Pascha puts forward:

The originators of the SME concept hoped for consensus to develop due to the implementation of policies in line with SME. Still, with their strong inclinations towards neo- and ordo-liberal ideas, they certainly did not have in mind the corporatist collusion of various associations and unions, enterprises and banks etc., which characterizes so many policy arenas of today's Germany (Pascha, 1996).

Accordingly, subsequent to practical implementation of Social Market Economy within German political economy, the concept has been circumscribed and knitted with its corporatist features and traditional socio-economic structures. Thus demarcating theoretical foundations of the concept from its practice has become complicated. Social partnership, industrial codetermination has gradually been “institutionalized throughout the Social Market Economy” and accordingly associated with the core elements of Social Market Economy concept (Ebbinghaus, 2002: 7). As Lehbruch indicates

The eclecticism made the doctrine of the Social Market Economy suitable to serve as a hegemonic discourse became particularly clear when its integrative capacity was no longer confined to the CDU and the “bourgeois” coalition. Beginning in the late 1950s, the Social Democrats, gradually abandoned the doctrines of democratic planning and came to accept the market economy, and this prepared the way for Karl Schiller to proclaim the synthesis of the “Keynesian message” and the “Freiburger imperative...A parallel movement, both labor and business gradually moved away from earlier antagonistic positions. The leadership of the employers’ peak association quite early advocated a social partnership approach involving organized labor, and when the unions gradually moved towards Keynesian positions, the implicit acknowledgement of macroeconomic interdependence paved the way for corporatist-style policy coordination...This, in turn, contributed decisively to the inclusion of organized labor in the core discourse coalition of the Social Market Economy (Lehbruch, 2005: 85).

This dynamic and flexible configuration of the concept has generated diverse interpretations and consequently created a kind of ambiguity. While some scholars and politicians remain loyal to the concept along with its original formulation by



Armack, which incorporates Ordo-liberal tenets such as market compatibility, the vast majority considers it as it was exercised in Germany in 1960s under the label of *Modell Deutschland*. In sum, the thesis suggests that diverse interpretations have reflected in the varying propositions of the EU institutions, namely the Commission and social partners in referring this two-fold concept, balancing market efficiency and social justice.

### **5.1.1 The Feasibility or Otherwise of Establishing Social Market Economy Order for the European Union**

With regard to analyzing the feasibility or otherwise of establishing Social Market Economy Order for European Union on the basis of original tenets of the Social Market Economy, it is considered that this type of analysis necessitates dealing with various comparison units with vast amount of information. For that reason, the thesis, by and large, concentrates on normative foundations and discursive function of the concept. Nevertheless, a broad framework within which the fundamental elements are mentioned is tried to be drawn.

Joerges and Rödl discusses that, there is apparently an aspect of an ‘economic constitution’ in the European Union implementations foreseeing the establishment a system of undistorted competition, an independent central bank, anti-discrimination rules, which are in line with Ordoliberal interpretations. Accordingly, the EU level provisions lays down a “law based order committed to guaranteeing economic freedoms and protecting competition with supranational

institutions” (Joerges and Rödl, 2004: 5). The supranational institutions were established in accordance with economic constitutionalism sought to prevent the political interventions. Consequently, it is seen that economic integrationist or one can say market making aspects of European integration were secured at the supranational level while social policy was left by and large to nation states’ hands. To that extend, “The social embeddedness of the market could and should be accomplished by the Member States in differentiated ways” (Ibid: 6). In this regard, one of the major theoretical cores of the Social Market Economy, namely Ordoliberalism, can be considered as relevant to the aspect of market making of the European integration. (Ibid: 5).

In reference to “social policy” aspect of the social market economy, it is seen that the application of the theory would differ in a union entity (EU) than a federal state (Germany). The popularity of the soft law mechanism and voluntary coordination in the European social field in comparison to the hard law instruments at the European level lessens the possibility of establishing uniform social and employment policies at the EU level. This is where the application of Social Market Economy at the EU level differs from the German case and constitutes one of the puzzling aspects of comparison. In the latter which is a federal state, there is not a demarcation in regulating economic and social sphere as the socio-economic order is overall regulated by binding national laws for both economic and social policy.

With the latest enlargement wave, the EU comprises of 27 national member states whose welfare settlements are diverging on a firm bases, as it was famously

elaborated by Esping Andersen and later re-defined along with the EU enlargement process by others. Following the globalization and post-industrial transition, national responses of member states given to the transformative pressures in diverse ways have been explored in many aspects. Some scholars intended to read the transformation of welfare state as a convergence towards Anglo-Saxon model since more market oriented approach has been adopted by most of the member states. (Mishra, 1999) On the contrary others deemed that the divergence of welfare arrangements within the Member states maintains its viability owing to the fact that diverging responses of national states to the external and internal challenges on the bases of diverse institutional framework of political economy (Manow and Ebbinghaus, 2001). The thesis contends that despite some scholars deems that varieties of capitalism will converge around Anglo-Saxon Model, the differences among Member States are still there and the Commission made a reference to Social Market Economy instead of referring to Anglo Saxon model of capitalism. In spite of the Commission's stipulation for a Social Market Economy as an attempt to demarcate the European socio-economic system from the US type, the existence of varieties of welfare capitalism in Europe might be regarded as one of the reasons complicating the application of a single Social Market Economy model at the European level.

### **5.1.2 Introducing Social Market Economy Concept in the EU Political Discourse**

According to the division made earlier in this chapter, after making an overview on the relation of original tenets of the Social Market Economy and European integration, now the focus will be on normative implications of the concept and its association with the political discourse of European Social Model.

There is not a concrete definition of the European Social Model; instead common substantive parameters are defined so as to designate a distinctive role to the “European” social model in comparison to the US Model of society and/or to pry out common values shared by various national welfare models”. By and large, the common parameters referring to substance rather than forms have been pronounced by the Europe’s political leaders in defining the European social model as “it is based on good economic performance, a high level of social protection and education and social dialogue”.<sup>11</sup> Jepsen and Serrano Pascual interpret the pronouncement of the European Social Model in the EU discourse as the reflection of the endeavors of the European Institutions to increase their “legitimacy based on identity formation”. By doing so, European social model comes to terms of being termed as a political project “as a way to identify these core values through which a European identity might be constructed” (Jepsen and Pascual, 2005: 240). Still, this identity building process would be raised more upon sharing of problems and

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<sup>11</sup> Above mentioned definition was made in Presidency Conclusions of the March 2002 Barcelona European Council. For more information, see A quick guide to EU employment and social policies, [http://ec.europa.eu/employment\\_social/social\\_model/index\\_en.html](http://ec.europa.eu/employment_social/social_model/index_en.html)

intervention solutions and less than common values. (Jepsen and Pascual, 2005: 240). Likewise, based on the above mentioned argument, it might be suggested that for being a political project, it would promote the welfare reform process in the name of “modernizing European Social Model” and framing the model by a comprehensive concept, Social Market Economy.

When the debates on the neo-liberal character of the European integration intensified and EU level unemployment soured, the tendency to re-word the European integration project so as to ease the tensions about the “social deficit” became more apparent. The concerns about the social deficit of the European Union emanated from the lack of European level market-correcting means decoupled seeing that the intervention of the European institutions in the social and employment areas regarded as having extensive neo-liberal character. In the wake of globalization and European integration, member states sought the ways of generating legitimizing discourses in order to provide “the public acceptance of the institutional and policy changes.” As Schmidt indicates;

Any such discourse will of necessity be quite different from one European Member State to the next, given the fact that Member States start from very different economic, institutional and ideational special cities, have responded to global and European pressures differently, and have, therefore, come up with different kinds of public discourses constructed by different mixes of elites (Schmidt, 2002a: 278).

At the European level, there occurred the affinity to compile different national discourses within a comprehensive framework so as to increase public adherence to the European Union. Accordingly, the next step can be considered as the establishment of a legitimizing discursive *framework*, knitted with “European”

core values, where the products of modernization of European Social Model could fit in and further stimulate the support of the European social partners and the consent of European transnational civil society via its “communicative function” (Schmidt, 2002a: 279).<sup>12</sup> Social Market Economy concept, ambiguous in definition, came to front as the most prominent notion where the discursive framework would be based on and a common platform for the intervention policies in the wake of welfare state transformation. The normative and empirical pronouncements of the Social Market Economy concept have been reproduced by both labor and pro-market elites to varying aspects. Diverse interest of labor and pro-market elites have formed the bases of differentiated contextualization of Social Market Economy seeing that the connotations deployed to the concept by various interest groups have been varied to a certain degree. It can be regarded that the Social Market Economy concept has been adopted so as to establish a common platform where social and labor market policy reforms could be rested upon on.

On the other hand, it can be observed that pivotal European social partners recently have come to the point of endowing the concept in their critics directed to censure the neo-liberal character of interventions at the European level. With regard to Economic and Monetary Union, the vast majority of the trade unions in the EU continue to refuse the neo-liberal restructuring notwithstanding their positions on Economic and Monetary Union in terms of supporting or, in contrary, rejecting the EMU (Bieler, 2006: 208). Andreas Bieler, by referring Strange, indicates that “in the vast majority of cases support for EMU was linked to demands of changing its

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<sup>12</sup> Vivien Schmit elucidates different functions of discourse one of which is communicative function aiming at persuading the larger public as to its merit (Schmidt, 2002a: 279).

neo-liberal implications. This understanding, that a single currency could be combined with a non neo-liberal, more employment oriented policy, is also reflected in scholarly assessments” (quoted in Bieler, 2006: 208). Accordingly, alternative policy mixes rather than neo-liberal policies have been proposed in light of enhancing the social dimension

#### **5.1.2.1 The European Commission’s Perception on Social Market Economy**

As it was discussed in the first chapter, the social dimension of the European was reinvigorated along with the initiatives of the Delors Commission with an attempt to regain a human face to the integration process as the economic integration revitalized after the signing of SEA. The political figures of the time placed more attention on the social dimension and suggested that European model of society should be knitted with the virtue of social cohesion constituted through balancing between economic efficiency and a degree of equality (Mitchell P. Smith, 1999: 37). Most importantly, the importance given to the role of labor unions and European social dialogue reflected the Commission’s attention in interest mediation and in embracing the broader interest for the European integration. As Tsarouhas puts forward through referring Apeldoorn and Gold, Delors inspired from the German Model of Social Market Economy and urged unions and employers to develop a European-level system of collective bargaining (Tsarouhas, 2007: 25). Streeck also states Delors’ inspiration of Social Market Economy in the sense that markets functionally necessitated to be “socially regulated”. (Streeck, 1996: 76) Many politicians, mainly Delors and his successor Santer, indicated that,

“especially with regard to continental models, there are significant similarities in European conceptions of society, of which the Social Market Economy is the most prominent” (Mitchell P. Smith, 1999: 38). However, as the economic agenda of the “1992 Project” gradually eclipsed the European social dimension, the distress concerning the neo-liberal character of the European integration has dramatically increased. Accordingly as Smith indicates; “With regard to legitimacy issue, the demand for a more robust social dimension and conflicting call for a neo-liberal single market have contributed to the new patterns of political mobilization and contestation at the EU level” (Ibid: 37). Social democratic coalition at the EU level maintained prioritizing employment policy and associated it with social cohesion.

The reference made to Social Market Economy by the Delors and in general by Social Democratic coalition can be considered as an inspiration from the German model of industrial relations and social system which is usually associated with the Social Market Economy. It is also important to note that the emphasis on the Social Market Economy was continued after the social democratic coalition was succeeded by more of a neo-liberal coalition in the European Commission. However, the substance of the meaning attributed to the Social Market Economy has been transformed. As Ross argued,

The social policy order of the day has shifted from constructing social regulatory policies at the European level, as attempted by Jacques Delor at the end of the 1980s and early 1990s, to reconfiguring labor market and other arrangements to allow European economy to compete in the world market (quoted in Holman, Van der Pijl, 2003: 79).

Along with the idea of modernizing the European Social Model, Social Market Economy concept has been adopted as a comprehensive framework within which



socio-economic institutions might be placed in and incorporated in the formal EU documents such as draft Constitution and Lisbon Treaty. Nonetheless, this time, the prominence of Social Market Economy has been more associated with market conformity and competitiveness instead of industrial relations. Furthermore, the role of the social market economy in competition has been highlighted by some of the Commissioners. Commissioner Monti stated in his speech at the Conference of the European Parliament and the European Commission on ‘Reform of European Competition law’ in Freiburg on 9/10 November 2000 that the role of the competition in a Social Market Economy as follows:

The concept of Social Market Economy stands for reliance on the market mechanism. It is based on the experience that the market mechanism is the most efficient way to meet the demand from consumers for goods and services. That the market mechanism will bring companies to increase productivity, to expand, to innovate – and to create jobs. In short, it recognizes that the market forces are the most efficient generator of prosperity. It therefore calls for a maximum of free market, for reliance on competition wherever possible...The liberalization experience of recent years at European level is in my view a striking example of how the courage to rely on the market forces is wanted today.<sup>13</sup>

Formally incorporating social market economy concept in the EU documents might be considered as the reflection of the augmented efforts to bridge the legitimacy gap. Aforementioned, the European Commission has adopted a new role in mediating the structural challenges and national responses. This is to be achieved by means of favoring the “positive effects” of globalization while averting its “negative impacts”. In Commission’s language, the Europe ought to become the most competitive and knowledge based economy, as this would be in compliance with the global structural change, and accomplish greater social cohesion while

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<sup>13</sup> For more information on the speech of Commissioner Monti, see: Competition in a Social Market economy, [http://ec.europa.eu/comm/competition/speeches/text/sp2000\\_022\\_en.pdf](http://ec.europa.eu/comm/competition/speeches/text/sp2000_022_en.pdf)

reproducing its traditional social consensus. Hereby, the very existence of a social market economy system at the European level would serve as a shield protecting welfare states from the negative effects of the globalization.

With regard to market efficiency characteristic of the Social Market Economy, it is seen that its discourse of “balancing market efficiency with social justice” is in line with the political discourse of the Lisbon Strategy as well as of the European Social Agenda emphasizing the essential linkage between Europe's economic strength and its social model while permitting positive and dynamic interaction of economic, employment and social policy. (EC.Europa, Social Policy Agenda, 2000). It envisaged the modernization of the European Social Model and “mobilization of the all key actors jointly towards new strategic goal” (Europa, Agenda for Social Policy, 2007).

Most importantly, the notion of flexicurity recently introduced in the European context is deemed relevant with the discourse of social market economy. Flexicurity is a new term that seeks to change the debate between the proponents of more flexible labor markets and the ones who aim to safeguard traditional security forms. The term flexicurity becomes very attractive in the academic and political debate since it seeks to resolve two apparently contradictory aims, namely flexibility and security (Nikolaus G. van der Pas, 2006)<sup>14</sup>. Starting with an academic interest on the remarkable flexibility and worker security witnessed in

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<sup>14</sup> For more detail on the speech of Mr Nikolaus G. van der Pas European Commission Director General for Employment, Social Affairs and Equal Opportunities on Where does EU social policy meet business?, see;  
[http://ec.europa.eu/ireland/press\\_office/speechespress\\_releases/vanderpasspeech\\_en.htm#\\_ftnref1](http://ec.europa.eu/ireland/press_office/speechespress_releases/vanderpasspeech_en.htm#_ftnref1)

the Dutch labor market during the 1990s, flexicurity soon became a catchphrase to be used by various actors such as the European Commission, European Parliament, and social partners. This widespread adoption reflects Europe's aim to incorporate a "human face" and to differentiate itself from neo-liberal labor market deregulation reforms that prevailed in American capitalism (Keune & Jepsen, 2007: 5-6).

The European Commission included flexicurity to the European Employment Strategy for 2005-2008 through Guideline 21, which calls member states to "promote flexibility combined with employment security and reduce labor market segmentation" (EC.Europa, European Employment Strategy). For Keune and Jepsen, it is not surprising that the Commission incorporated this term. Accordingly, this adoption arises from the Commission's; "knowledge disseminator role", "role as broker between interests", and its "discourse on European Social Model" and on the linkage between competitiveness and social cohesion. Thus, it should be emphasized that flexicurity is employed by the Commission as a "powerful discursive tool" so as to enhance its influence on member states (Keune & Jepsen, 2007: 9). As Ross indicates:

The Commission itself is an interest group in favor of more integration, an agitator and a planner for a more European future. One can phrase this in a noble, "Monnet-like" way to justify the Commission's activities as being in all European's interest. Or one can be more down to earth and see the Commission as an ambitious institution trying to expand its mandate and increase its role. This is probably more close the reality (Ross, 1997).

Accordingly, the thesis states that by means of introducing Social Market Economy, the Commission would have the occasion to generate "unity in

diversity” through setting up a normative framework knitted with common core values transcending the socio-economic institutional differences in national member states while strengthening its position for being one of the leading European institutions.

Moreover, it is acknowledged that the discourses of the European institutions considerably impose “socio-cognitive influence” on national policies member states adjust these policies in line with reference frameworks proposed by the European institutions (Jepsen and Pascual, 2006:11).

#### **5.1.2.2. European Social Partners’ Perception on Social Market Economy**

As the debates about social Europe substantially increased, it is observed that European social partners, namely ETUC and EPSU, started to integrate the Social Market Economy notion in their discussions circling around European social sphere.

Social partners and trade unions involved in the debates on the future configuration of the EU held before the Intergovernmental Conference in 2003. There, the representatives of ETUC stressed the importance of endowing the principles of Social Market Economy “by way of a basic treaty reference, instead of the current reference to “an open market economy with free competition. This vision is one of a Social Market Economy, i.e. an economy where the role of the market is recognized but where this market is controlled by means of social regulation”

(Degryse; 2002). It striking to see the contrast between the Commission and ETUC as well as EPSU in their position of Social Market Economy. While the former focuses more on market efficiency, the latter emphasizes social aspect of the Social Market Economy.

ETUC in its memorandum to the Austrian Presidency of the European Union in January 2006 makes a reference to Social Market Economy and indicates the importance of getting the revised Lisbon Strategy back on the right track as they asserted that the Lisbon Strategy of 2000 was imbalanced in terms of social cohesion and market efficiency and made the mistake of “seeking economic reforms just for the sake of the reform”. They continued that;

The concept of Social Europe must be central to the development of the European Union where economic and social progress must go hand in hand. The balance between the two should be struck without hesitations and, within an enlarged European Union and a globalised world; the European approach must be the promotion of a Social Market Economy, with social rights (ETUC, 2006)

In light of the abovementioned statements, it can be concluded that the reference of these social partners to Social Market Economy can be much more associated with the views of Armack and more likely the second stage of its implementation corresponding to expanded social partnership rather than Ordoliberal interpretation of the concept. As mentioned at the fourth chapter, Ordoliberals put more emphasis on the limited role of intervention seeing that true functioning of ordered based market would favor the social ends, and social intervention, at any rate, should be in compliance with market functioning. Besides, it can be considered that their position to Social Market Economy as an ideal European model can be seen as an

attempt to appraise the tendencies towards being more market oriented rather than equilibrating between market efficiency and social justice.

In the EPSU position on, then proposed Communication of the Commission on the Internal Market Strategy Priorities 2003-2006; it is stated that “EPSU, together with the European Trade Union Confederation, has supported the completion of the Internal Market as an instrument to foster growth, employment and a higher level of welfare for all citizens.” However, it is alleged that the focus of Strategy was on structural reforms and liberalization of markets and further competition and the social dimension was missing. Thus; “The impression is given in the Communication that a policy is pursued of forced liberalization”. In the position paper, EPSU indicated that

The proposed “Internal Market compatibility test” appears to be an attempt by DG Internal Market and its Commissioner to give priority to the internal market and competition rules over other objectives within a socially balanced market economy... Instead of an Internal Market Compatibility Test, a test is needed that takes account of the whole range of EU objectives, including employment, sustainable development, equality, and social and economic cohesion. For lack of a better term EPSU calls this: the Social Market Compatibility Test (EPSU, 2003)

European employers’ view with regard to incorporation of Social Market Economy in the Draft Constitution was relatively critical seeing that they consider Social Market Economy concept “linguistically ambiguous” and unclear in definition. Georges Jacobs, on behalf of UNICE, called for the reference to the Social Market Economy to be deleted, on the grounds that there was no consensus on this matter (European Convention, 2003). In this regard, Streeck points that; “European employers have no interest in advancing positive integration or European level

social intervention; with respect to common social policies that go beyond market-making” (Streeck, 1996: 70).

Overall, it can be concluded that different interest formations at the European level emphasize various aspects of the Social Market Economy theory. Furthermore, this is not so much a matter of wrong interpretation, but can be considered as attempts to construct, albeit sometimes discursively, an agreement on various issues.

## **CHAPTER VI**

### **CONCLUSION**

In the thesis, the European vision for a “Social Model” with regard to its correlation with the notion of Social Market Economy has been explored. Accordingly, the thesis has been built upon three subject matters, namely the history of developments in the European Social Dimension, the theory of the Social Market Economy and the association between European Social Model and Social Market Economy.

The European integration project is primarily commenced as a liberal economic integration aiming to eliminate trade barriers and to establish a common market. The development of European level social policies was subordinated to the process of economic integration and the competence in regulating the social policy realm remained at the hand of national member states. The limited role employed to the EU level social policies were by and large dealt with facilitating the formation and well functioning of the market.

However, as the economic integration intensified especially from the 1990s onwards, it started to influence the ways in which labor markets functioned with important implications for the conduct of industrial relations and the pursuit of social policy in the member states. With the introduction of the EMU and the



establishment of the European Single Market, increasing number of national policy domains -including social and labor market policies- have been exposed to the consequences of this integration. In consequence, room for national maneuver on social policy has gradually been limited.

Most importantly, the period starting from the early 1990s to present has been regarded as the era of welfare state transformation due to intensified international competition, post-industrial transition, changes in demographic parameters as well as household patterns and finally increased European integration. In this regard, it is contended that in consequence of both the impact of European integration itself and its circumscribing affect on national social policy regulation, the role of national member states to mitigate the social risks emanating from post industrial transition and globalization has been decreased. Accordingly, the concerns about the “social deficit” of the EU have intensified.

In due course, the discussions revolving around the “modernizing” European Social Model appeared at a time when pressures emanating from globalization, Europe led deregulation and post industrial transition challenged the existing welfare arrangements. In spite of the diverse welfare regimes within the European Union, the challenges affecting the welfare systems were similar. Consequently, European Union has adopted a new role in designing the European social sphere subsequent to the Lisbon Summit of 2000. “Being more competitive while ensuring greater social cohesion” has become the new motto of the EU. Eventually, new approaches and tools have been developed so as to attain the targets of Lisbon Strategy.

The development of European social dimension has coincided with different modes of political economy due to the transition from embedded liberalism to Neo-liberal paradigm. Accordingly, the role and the vision endowed to the social and labor market policies in the post war period have transformed both at the national as well as the EU level.

With the growing dominance of the Neo-liberal paradigm, supply side policies such as active labor market policies replaced the Keynesian demand management techniques. Thus, welfare states are came to be seen as “active welfare states”, responsible for the promotion of employability rather than full employment. The traditional role of welfare state in decommodifying labor, to an important extent, turned into the recommodifying and increasing the employability of labor consistent with the changing political economy and post industrial transition. Accordingly, the Commission’s vision for European social policy as “by product of economic policy” has been replaced with an approach of “social policy for being productive factor”.

The process of European social policy making has been supplemented with additional methods. EU sought the ways of generating common understandings of the problems in the wake of welfare state transformation and mitigating the member states’ interventions in the policy reform. Therefore, a new approach; entitled Open Method of Coordination has been developed firstly in the field of the employment policies and later for social inclusion and pensions so as to overcome the constraints of existing community method. In the Rome Treaty, the reference

was made to social policy had foreseen the harmonization of national social systems. The European approach to social policy making by means of traditional community method has been, to an important extent, redefined with a dictum of “unity in diversity” and supported by a *coordination* narrative seeing that the number of members states with diverse welfare systems- from six founding states to twenty-seven members- has increased and the reluctance of most of the member states to delegate more competence to the EU in the social policy realm has continued (Streeck, 1995). The path and the means of social policy within European integration have changed from deepening to extending in scope. That is to say, there is increased use of soft policy measures instead of legal regulations, and they are disseminated to more social policy fields (Kvist, 2004: 303).

Overall, the EU has developed new tools such as Open Method of Coordination and Flexicurity so as to promote policy reform as well as to mitigate the diverse responses of the national member states given to the aforementioned challenges. Accordingly a new discourse, formed around Social Market Economy, was incorporated in the formal EU documents namely the Draft Constitution and Lisbon Treaty of 2007 so as to mobilize the actors at the European as well as national level for policy reform and stimulate the support to the new vision on “Social Europe”. In this regard, Social Market Economy, being an “irenical concept”, can be argued to be utilized as a comprehensive framework where different aspects of European Social Model could be placed in. The terminology of Social Market Economy, knitted with normative connotations and blurred with various interpretations, was chosen to reproduce the historical commitment of the European welfare state on

providing high level of benefits, and substantial social dialogue throughout post war period.

The idea behind the creation of the Social Market Economy was that this type of market economy would be equipped with social safeguards which are in conformity with the market and therefore would balance the market outcomes for the sake of social justice. According to Leipold, generating a comprehensive welfare state was not the inspiring point for establishing Social Market Economy (Leipold, 2001: 341). Still, by the mid 1960s, welfare state policies increased in line with changing economic and political conjuncture with the extension of interest representation of labor and increased social security provision. Accordingly, government intervention in the economy to redistribute the outcomes of the market expanded and the issue of state intervention seems to blur in practicing the Social Market Economy. Consequently, the social phase of the concept was started to be reinterpreted along with the in German economic and political history.

In analyzing the Social Market Economy concept at the EU level, a separation is made between feasibility of adopting the original tenets and endowing normative connotations employed to the concept in the political discourses. A general comparison between German case and the EU in terms of practically applying the concept is tried to be made. Because of the varieties of capitalism existing within Europe as well as the substantial differences between practicing the theory in a federal state and in a union entity with multilevel governance system, the comparison units happen to be different. Thus, the focus is more on the normative

connotations of the concept, the political discourses of the related actors in the EU level are explored.

As mentioned above, the concept of Social Market Economy is ambiguous and open to various interpretations. This peculiarity gives the opportunity to diverse institutions and interest groups to utilize the concept in the pursuit of varied goals. It may be argued that European Commission uses Social Market Economy within its endeavor to legitimize the process of the modernization of European Social Model. Accordingly, the concept has been operated as a general framework where the outputs of and the tools for modernizing the European Social Model could be placed in. Most importantly, the endowment of the concept by the Commission reflects the attempts to differentiate the European style of adaptation to structural changes in the wake of post industrial transition as well as globalization then the US style.

In addition to this, defining the ‘other’ by means of generating a coherent European political identity that is cognitively constructed upon the concept of Social Market Economy also serves to increase the adherence to the European integration process. By doing so, the Commission also seeks to increase its influence as a broker of interest. As Jepsen and Pascual states, “the nature of European integration lies in the production of common notions and concepts, despite the different institutional settings and political values across Europe” (Jepsen and Pascual, 2005: 240). Consequently, the Social Market Economy might be envisaged to contribute easing the tensions about the vague future of the Social Europe as well as

promoting policy reform in response to changing economic conditions by means of consensus building on economic and social progress, notwithstanding its ambiguous nature developed due to different connotations attributed to the concept by many scholars and politicians.

Finally, it can be stated that, when it comes to 2005, the implication of the Lisbon strategy started to be criticized for being more market efficiency oriented rather than socially balancing by ETUC and EPSU. Accordingly, in their political discourse social market economy notion has gained the function of criticizing the neo-liberal character of the implications of the Lisbon Strategy.

Overall, the thesis argued that Social Market Economy has being used as a comprehensive discursive framework by various European actors to varying aspects. This arises from the ambiguity of the concept itself as well as its normative elaborations.

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