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Lower coverage but stronger unions? Institutional changes and union wage premia in Central Europe

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ABSTRACT

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In this paper we use the national samples from the European Structure of Earnings Survey (ESES) to analyze the evolution of the wage premium of firm- and industry-level agreements in the Czech Republic, Hungary, and Poland (the CE3) around the time of their accession to the EU. We find that despite a generalized reduction in union coverage in these countries, the union wage premium after accession to the EU became bigger and statistically more significant for Poland and Hungary, particularly for industry-level agreements. We interpret these findings in terms of the institutional reforms that occurred in the CE3 between 2002 and 2006. These reforms, which were prompted by the EU Commission's requirements for EU accession, increased the social partners' ability to bargain and enforce wage agreements, and made industry-level unions more effective in guaranteeing the protections provided by labor standards. Results are less conclusive for the Czech Republic, probably due to factors that attenuate the effect of bargaining coverage upon wages, e.g. a smaller effect of institutional reforms, a greater use of mandatory extension mechanisms, the more radical firm restructuring during transition in that country. *Journal of Comparative Economics* **44** (3) (2016) 638–656. Warsaw School of Economics and Institute for Structural Research, Poland; Centre for Economic Performance, London School of Economics and Political Science, United Kingdom;Dipartimento di Economia e Finanza, Università Cattolica di Milano, Italy and Centre for Research in Economic Analysis, Université du Luxembourg, Luxembourg.

1. Introduction

The extensive reforms of labor market institutions that occurred in Czech Republic, Poland and Hungary (the CE3) in preparation for accession to the European Union were widely expected to have a profound impact on the organizational strength and bargaining power of trade unions and employer organizations in these countries. From the early 1990s, the transition to a market economy paved the way for a process of union "revitalization," which was signaled by the existence of union wage premia in newly established private enterprises (Magda et al., 2012). Starting in the early 2000s, the prospect of accession to the EU

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triggered extensive institutional reforms in the CE3. In its 1995 White Paper, the European Commission stated explicitly that the implementation of these reforms was a prerequisite for entry into the EU (European Commission, 1995). The objective of these reforms was to improve the dialogue between the social partners, establishing a role for the government in a tripartite concertation mechanism, and enforcing labor standards comparable to those of the existing EU member states (EIRO, 1998). In addition, the participation of CE3 policy makers in the EU's *Open Method of Coordination* in the area of labor market policy was also expected to help these countries reshape their national labor market institutions so that they more closely resembled the institutions of the EU15 member states. As these discussions and exchanges of good practice placed a strong emphasis on the involvement in policy-making of unions and employer organizations, it was anticipated that the influence and bargaining power of these social partners would be enhanced.

The effects of these extensive institutional reforms on the structure of wages in the former transition economies of Central Europe are still largely unknown. Yet this issue appears to be important given the declining union density and collective bargaining coverage observed in the majority of new EU member states in the early 2000s (European Commission, 2010). In this paper, we seek to shed new light on this question by analyzing the wage premium of collective agreements in the Czech Republic, Poland, and Hungary in 2002 and 2006, 2 years before and 2 years after their accession to the EU in 2004. These countries are characterized by a model of collective bargaining which lies somewhere between the Anglo-Saxon and the western European models. It presents a form of national-level social dialogue consisting of worker and employer representative organizations, which deliberate on improvements in employment legislation and on the scope for national increases in pay. This system combines firm-level and industry-level pay agreements, a national minimum wage, and a labor inspectorate that oversees the enforcement of labor rights and employment contracts. Unlike in some western European countries, where individual firms may be subject to both industry- and firm-level agreements, (e.g., Italy, France, and Germany), in the CE3 model there is no overlap between firm-level and industry-level pay agreements, and a large share of the workforce is employed in firms not covered by either type of agreement.

As discussed by the recent literature on the new varieties of capitalism and welfare (see e.g. Bohle and Greskovits, 2007), the CE3 are of particular interest among former transition economies from Central and Eastern Europe (CEE) for at least two reasons. First, they are the earliest reformers among the post-socialist economies of Central and Eastern Europe, and differently from other CEE countries (e.g. Romania or Bulgaria), they entered the 2000s with collective bargaining systems that were deemed sufficiently mature to implement the reforms required for EU accession. Second, they were the first post-socialist economies to join the European Union (in 2004). Thus, we can assume that the experiences of the CE3 provide a valid benchmark for future EU accessions.

We use data from the 2002 and 2006 waves of the European Structure of Earnings Survey (ESES), a unique cross-sectional linked employer–employee dataset provided by Eurostat. The availability of the 2002 and 2006 ESES waves allows us to compare the characteristics of union wage premia 2 years on either side of the EU accession year of 2004. It is reasonable to assume that any changes in the structure of the union wage premium which occurred during 2002–2006 were strongly associated with major institutional changes linked to the accession.

With this study, we are contributing to the literature which has analyzed the effect of institutional changes on the union wage premium and wage inequality. Existing research has focused on changes in western (mostly Anglo-Saxon) economies. Fortin and Lemieux (1997) analyzed the impact of institutional decline on the rise in wage inequality in the United States during the 1980s, and showed that the de-unionization and minimum wage decline were responsible for about one-third of the increase in male and female wage inequality. Gosling and Machin (1995) and Machin and Manning (1994) analyzed the contribution of declining unionization to increasing wage inequality in Britain between 1980 and 1990. They showed that the decline in the share of plants with a recognized union accounted for around 15% of the rise in earnings inequality during the period. Koeniger et al. (2007) used aggregate data to investigate how the changes in labor market institutions affected wage inequality in 11 OECD countries between 1973 and 1998. They found a consistent reduction in male wage inequality in countries (e.g., France) where minimum wages increased and employment protection became stricter, but increased inequality in countries (e.g., the United States and the United Kingdom) where unions became less powerful and minimum wages fell. To the best of our knowledge, this study is the first to look at the effect on the structure of wages in post-socialist economies of institutional changes which have had an impact on the power of unions. In particular, our focus on the years 2002 and 2006 allows us to concentrate on the wage effects of institutional changes that occurred during the accession of these countries to the European Union.

2. EU accession and the institutional setting of CE3 countries

An essential element of the transition from a centrally planned to a market economy is the development of labor market institutions that determine how firms and workers negotiate employment contracts and revise terms of employment. In the three countries examined in this paper, the transition to a market economy occurred in two main stages: the immediate institutional changes that came about after the fall of the Iron Curtain in 1989, followed by accession to full membership of the European Union in 2004. The first stage of the post-1989 transition involved a large-scale shift to privately owned enterprises, and the initial establishment of new social partner organizations. In contrast, EU accession involved more far-reaching changes to labor market institutions, in part to bring them into line with the EU employment legislation, and in part to adapt them to the European single market.