Austerity and the demise of Social Europe:

The Baltic Model versus the European Social Model

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**Abstract:** This article draws on the experience of the imposition of radical austerity measures in the Baltic states. It challenges the myth that austerity can be achieved in a socially and economically ‘costless’ manner. Baltic-style austerity has now become a template of ‘successful adjustment’ and a recipe for recovery for the Eurozone. The authors argue contra such ‘myth-making’ that austerity is compromising the longer-run sustainability of societies that follow this path, whilst simultaneously ending prospects of the adhesion of a European ‘Social Model’ in the post-communist periphery. The article is a contribution to an emerging debate in academic and policy circles concerning the viability and future of Europe’s ‘Social Model’ in an age of austerity.

**Keywords:** Austerity, crisis, Baltic states, European Social Model, internal devaluation, neoliberalism, Social Europe.
Introducing the specter of Social Europe

European labor now finds itself in a profoundly weakened position in the aftermath of the Great Financial Crisis (Busch, Hermann, Hinrichs & Schulten, 2013; Bernaciak, Gumbrell-McCormick & Hyman, 2014). Economic trends long underway in the global system since the demise of the Bretton Woods order in the 1970s have rapidly accelerated in the wake of the 2008 financial crisis. Europe’s long-standing corporatist structures built during the Bretton Woods system have been maneuvered into ‘concessionary’ stances leaving organized labor largely unprotected from the imposition of austerity policies (Bieling & Lux, 2014).

European Union fiscal and monetary policy, by institutional design, have made its constituent member countries vulnerable to economic crisis, and once in crisis, have limited their ability to expedite recovery, other than on terms set by those promoting economic competitiveness over social considerations. Given these constraints, it has become crucial to identify and promote a model of austerity management which can be proclaimed a ‘success’ in the face of rigorous fiscal consolidation. The three Baltic states of Estonia, Latvia and Lithuania have served as such exemplars, celebrated by the European Central Bank, the international financial community and its attendant commentators. In the words of the eponymous editor of Forbes magazine, unlike their unruly Southern European brethren, the Baltic states are the ‘unsung heroes’ of the crisis, enduring painful austerity measures without social upheavals (Forbes, 2010).

The story of Baltic austerity has been amplified in what has become a manual of austerity management, authored by no less a person than the then Prime Minister of Latvia, Valdis Dombrovskis, in a collaborative panegyric with the Swedish economist Anders Aslund from the ultra-neoliberal Washington-based Peterson Institute, in a joint work entitled with deceptive modesty How Latvia Came through the Economic Crisis (Aslund & Dombrovskis, 2011).
Our purpose is to contest the narrative of austerity ‘success’ as a ‘myth-in-the-making.’ In so doing, we suggest that austerity measures adopted by the Baltic governments have created societies that are, in terms of foreseeable prospects, neither socially sustainable nor capable of enduring economic recovery. This alternative narrative is part of a wider European story in which the core and periphery have been irreversibly torn asunder by the crisis. In terms of the grand European project of eventual integration, the Baltic states have been full members of the European Union since accession in 2004. With a collective population less than that of London or Moscow, these three tiny post-Soviet states might hardly merit more than a momentary reflection. That is, except for one awkward fact, that the protections of a shared European Social Model (balancing unrestrained market forces by a ‘social dimension’) which in times of crisis can mitigate the impact of market failure, have proved elusive for these populations of Europe’s periphery (Whyman, Bambridge & Mullen, 2012).

The transfer of a putative Social Model eastwards to the new post-communist member states of Eastern Europe was a problematic process from the inception of accession negotiations in the early 2000s. In the new market economies of Eastern Europe organized labor has been unable to impose a historical compromise on capital in terms of securing an effective social dialogue between labor and capital, or a broad commitment to a social welfarist society such as that which prevailed (at least temporarily) in advanced Western social democracies (Bohle & Greskovits, 2012). Even in its heyday therefore, this model was more compatible with advanced Western social democracies, while today it has been all but eviscerated (Hermann & Mankhopf, 2010; Hermann, 2013; Vaughan-Whitehead, 2014).
The European Social Model’s ill-defined normative thrust towards socially redistributive policies, and its unevenly developed institutional configurations in terms of the ‘hard’ law of the European *acquis* and accompanying Directives, made it less than robust as a vehicle for European integration (Zahn, 2013). The new pro-market elites of the post-communist Baltic states in their eagerness to attract inward foreign investment adopted neoliberal prescriptions following the collapse of the USSR, with low controls on capital, open markets, reduced provisions for social welfare and depleted labor rights (Bohle & Greskovits, 2012). European Union membership, desired in terms of market opportunity, was viewed in social policy realms as implying unwelcome ‘Brussels interference’ in areas such as employment and welfare that were to remain largely the prerogative of national governments (Lendvai, 2008).

Europe’s Social Model as an overarching integrationist project therefore was under strain before the current period of crisis and austerity, challenged not least by the very divergence of social welfare and industrial relations ‘models’ within the European space. The accession of new EU member states from Eastern Europe underscored and reinforced a longer-term shift in priorities in European-level policy-making towards an agenda favoring market-driven criteria over social considerations. In this reconfiguration of social and economic dimensions of the EU project, a key role in undermining convergence in labor standards was played by the European Commission itself in promoting labor ‘flexibility’ under the guise of ‘modernization’ of labor markets and in the impetus this provided towards the progressive scaling back of employment protection legislation (Sciarrà, 2007). It is in this sense that the European Social Model, seen as a configuration of social dialogue in the workplace and wider social protection measures ultimately rooted in national models, was redefined by neoliberal governance even before the onset of the current crisis (Song, 2011). Since the crisis, national models, especially where employment protections are only weakly articulated
as in the post-communist periphery, have further crumbled in the face of the new austerity offensive against labor and social rights orchestrated by the Commission in tandem with national governments (Heyes & Lewis, 2014).

Yet at the very moment of its nadir, the specter of a ‘Social Europe’ has been resurrected by the European Commission as a panacea for repairing damaged social cohesion resulting from crisis and austerity (Kvist, 2013). The framing of the experience of austerity in the Baltic States in the context of this debate is therefore neither innocent nor without important implications for viable policy options for recovery in the wider European periphery. The article proceeds as follows: first, we interrogate the notion of Baltic-style ‘internal devaluation’ and assess the veracity of the narrative of ‘necessary sacrifice rewarded’. Second, the effect of fiscal adjustment in terms of propelling a mass migratory exit of a new *austeriat* is identified as the most damaging social cost of austerity in the Baltics. Third, broader political and economic issues concerning macroeconomic imbalances and the role of the euro in limiting alternative policy responses to the crisis are reviewed. Finally, the question of the feasibility of a renewed European Social Model is posed against the prospect of continuing austerity.

**Crisis and internal devaluation in the Baltics**

The primary ‘path-dependent’ source of the 2008 economic crisis in the Baltic states was their mutual embrace at independence in 1991 of the then globally ascendant neoliberal economic development path. The decision to de-industrialize and liberalize their economies represented a shift from developmental state policies to those of comparative competitive advantage (Viksnins, 2008). For the Baltics, ‘comparative advantage’ primarily meant being made offshore finance and transit economies, both of which exaggerate cycles of economic
booms and busts, and providing reservoirs of flexible and cheap labor for export (Becker & Jäger, 2010).

With EU accession in view investment poured in due to several interrelated factors: 1) a global avalanche of money created by the US Federal Reserve and Japan was made available (through a ‘carrying trade’) to the Baltic states via Swedish banks. New mortgages loaded down property with debt, which at the same time created a property bubble; 2) the increase in global commodity prices (especially oil and metals) stimulated by demand from China and India (plus the invasion of Iraq in 2003 by the Bush administration, which pushed up oil prices) in turn, drove Russian cash offshore (tax dumping, money laundering) to its Baltic ‘near abroad’; 3) EU Structural Funds poured into these new EU member states in the mid-2000s matching and underwriting increased confidence in the Baltic states by Western investors generally. This flood of money lifted these economies on the crest of tidal waves of finance, which then crashed with punishing force following the global crisis of 2008. (See Figure 1).

Figure 1. EU and Baltic GDP Growth Rates, 2005-2014
The crash brought in its wake a severe ‘correction’ in property prices (up to 70% of pre-crisis nominal values). All three Baltic state economies were hit with double-digit sized contractions of GDP. Lithuania saw real GDP declines (price adjusted) of 14.8%, Estonia 18.3%, and Latvia experienced the sharpest real GDP drop of any country in the world of 21.8% between 2008 and 2010 (Eurostat, nd). For Baltic governments the outlook in 2008 was bleak. Latvia’s debt to GDP ratio was 18.6%, Lithuania’s was 15.4%, although Estonia, which entered the crisis with public finances in better order, was a mere 3.7% (compared to Greece at over 100%) (Trading Economics, nd). At this critical juncture, the governments of the Baltic states had a choice: either to mitigate economic hardship inflicted on its people to the degree possible, or to use the crisis to further liberalize the economy and increasingly integrate into the EU. The latter option was chosen which also meant pursuing entry to the eurozone group of member states adopting the common European currency (at all costs), which in turn foreclosed monetary stimulus, debt write-off or national currency devaluations.
In order to meet the fiscal and monetary criteria for euro adoption, so-called ‘internal devaluation’ was selected as the preferred policy choice, thereby maintaining currency pegs to the euro.

The effect on employment and income levels was profound. Labour carried the burden of the crisis in terms of indirect and income taxation (high tax wedges for low income earners) as well as mass unemployment, reduced living standards and depleted social welfare provision. Real wages declined on average by 5%–8% in 2009 and 2%–6% in 2010. The decline in real wages was largely halted in most of the EU in 2010, but in Latvia only in 2011, and in Lithuania only by the end of 2012. Coming in the wake of extraordinary wage growth during the boom years of the ‘Baltic Tigers’ in the mid-2000s, this decline of real wages is an indication of the labor market’s ‘flexibility’ and the overall disempowerment of labor. In 2009 and 2010, public sector wages were cut more than average private sector wages, dropping by 18% in 2009 and by a further 9% in Latvia in 2010, and around half of that in Estonia and Lithuania. While reductions in employment in the public sector occurred (20% in Latvia 2010), the private sector bore the brunt of job losses. Official unemployment rates in the Baltic countries were the second-highest in the EU after Spain, reaching 17%–19% in 2009. Youth unemployment rates soared to over 30% in all three Baltic countries. While rates have declined since, this is partly a function of mass emigration. For those who have remained, the share of long-term unemployment in total unemployment was 48.5% in Latvia, and in Lithuania and Estonia, 41.4% and 40.9% respectively in the last quarter of 2013 (SEB, 2014).

The austeriat

The suppression of wages and mass unemployment did not act as a trigger for social protest
on a large scale. One reason for this is that the Baltics possess the lowest levels of trade union density in the EU. National union leaderships relied on formal representational mechanisms in tripartite forums including government and employers, while bipartite social dialogue and collective agreements at the workplace have been perilously weak. Sporadic protest actions undertaken by trade unions in all the Baltic countries during the crisis were not successful in mobilizing more broadly-based societal opposition and largely fizzled out in sectional protests by teachers, students, fire fighters, pensioners and parents’ groups. These were increasingly met with administrative obstructionism and hostile policing (Woolfson, 2010; Juska & Woolfson, 2013).

The onslaught of austerity policies undermined the remaining collective confidence of labor, while an ‘illusory corporatism’ trapped leaders of trade union confederations in national tripartite ‘peace’ agreements, offering to suspend protests in exchange for moderation of cuts to welfare and employment. Such agreements were largely overridden by Baltic governments bent on crisis-driven reforms, including weakening employment protection provisions in labor codes and pension and social welfare cuts (Kallaste & Woolfson, 2013). In the private sector, at workplace level, new more flexible contractual arrangements allowed employers the opportunity to effect redundancies more cheaply and quickly, and to substitute temporary for full-time contracts while imposing less favorable working conditions. Payment through undeclared ‘envelope wages’ in an informal economy became common again after a period of decline. In Latvia for example in 2013 an estimated informal economy amounted to 23.8% of GDP (European Commission, 2015b, p. 12).

Denied meaningful ‘voice’ in both the workplace and society many, particularly the unemployed, selected the ‘exit’ option. ‘Free movement’ of labor turned into a veritable
‘exodus’. This Baltic austeriat could be characterized as a specific ‘variety’ of a broader though somewhat ill-defined and contested notion of the ‘precariat’ (Standing, 2011; Bremen, 2013). The austeriat points not just to a generalized condition of precarity but to the concrete socio-historical causes and consequences of austerity policies in producing dis-located labor migrants compelled to use mobility not so much as an economic opportunity, but as an economic survival strategy in times of economic crisis. It identifies those from whom the crisis has exacted an especially heavy toll in terms of unemployment, labor informalization and reductions in living standards and for whom ‘exit’ appears a possible escape route out of impoverishment and austerity (See Figure 2).

Figure 2. Crude Rate of Net Migration plus Adjustment from Baltic states, 2004-2013

Lithuania and Latvia have been at the forefront of EU countries with the highest negative net
rates of migration while Estonian emigration has been muted by the ability to commute to Finland for work (OECD, 2013). Net migration from Latvia reached −17.0 per 1000 population, and in Lithuania −25.2 per 1000 population at the height of the crisis (although the later number was inflated by changes in domestic insurance registration procedures). In 2009–2010 alone, emigration reduced the size of Latvia’s population by 3.6% and Lithuania’s population by 3.3%. In all, while exact numbers are difficult to provide, in excess of some 10-12% of the workforce has departed and while there has been increasing return migration, the negative net flow continues (ELTA, 2013).

Not all have chosen the ‘exit’ route, but those who did so have included disproportionate numbers of younger workers (20 to 35 years of age), individuals who had been unemployed for more than a year, and increasingly whole families with young children. The result in demographic terms is that by 2060, the share of the population aged 65 or more is projected to reach 35.7% in Latvia producing an old age dependency ratios reaching 68%, both figures the highest in the EU (Eurostat, 2011; Eurostat, 2011, table 2). At the same time, Lithuania’s general population is currently the most rapidly declining in the EU as a result of the combination of outmigration, low fertility, low life expectancy and high morbidity rates with up to three quarters of that decline accounted for by out-migration (European Commission, 2015).

The shrinkage of population however has not been uniformly spread in geographical terms. Within the depleted populations of the Baltic periphery there is an uneven pattern in which the periphery within the periphery has seen disproportionate decline, while capital city regions have remained less affected. The fastest population decline per annum in EU in 2011 was reported for Šiaulių county (-22.7 per thousand) in northern Lithuania, close to the
Latvian border. It is in such peripheral regions the highest levels of poverty, long-term unemployment and welfare dependency are to be found. Here the remaining economy is increasingly organized along informal lines, supported by a substratum of illicit alcohol manufacture and cross-border smuggling. Traversing these bleak flat agricultural wastelands are newly refurbished highways, courtesy of EU Structural Funds whose generous disbursement is gratefully acknowledged by ubiquitous European Union blue-bannered billboards. Erected at the side of one such road on the way to the Lithuanian border with Latvia, the billboard proclaims (in Lithuanian): *Together we are creating Lithuania’s future!*

Emigration on this scale produces a hemorrhaging of human resources necessary for rebuilding post-crisis economies and society. Orderly labor markets and balanced social and economic development have departed from the Baltic states. This demographic cost of austerity does not appear on the balance sheets of Western European banks and financial institutions. From a strictly Malthusian standpoint emptying the impoverished Baltics to leave a residue of pensioners, long-term unemployed or those who simply cannot move, is hardly in itself a prescription for a European catastrophe other than on a localized scale. And yet, given the pivotal importance ascribed to the Baltic model of austerity management, it is worth restating that the societal costs entailed are not merely a localized or transient phenomenon. In the actually existing world of neoliberal austerity these costs are replicated, to a greater or lesser degree, across the European periphery (Leahy et al., 2015). Weighing such costs against the benefits of a single monetary union is an issue upon which the future of Europe may depend. For the three Baltic countries however, euro membership was deemed unproblematic by its governing elites and a precondition for their further European integration.
The Euro and Contested Baltic recovery

In the Baltic states, the euro, while not in place during the run up to the crisis, was nonetheless the preferred currency for mortgages, delivered by mainly Swedish banks at the lower interest rates carried by the euro as opposed to national currencies. This contributed to asset price inflation, but also complicated policy choices in the aftermath of the crisis. The standard policy option for countries in such a situation would have been currency devaluation. This choice, however, would have greatly inflated the value (and debt burden) of euro loans. An alternative would have been to redenominate euro loans into local currencies, followed by devaluation. Yet this would have represented a de facto write-off of a significant volume of indebtedness, fatally compromising the strategic economic (and political) goal of the Baltic elites to secure early euro accession and the perceived need to ensure continued foreign capital inflows. The Baltic states were determined to avoid the trap of government borrowing that frequently follows the collapse of a private foreign credit-fuelled bubble and the accompanying exit of that easy money. Thus, their governments responded by imposing an austerity program so chastening in its severity that it would avoid the public debt trap that befall many other nations in the past when private credit dried up (Streeck, 2011).

These policy constraints led to the embrace of ‘internal devaluation,’ a policy option known in theory, but not put into practice in the context of post-war Western European democracies given the significant risks to social cohesion posed by massive unemployment and draconian cuts to social benefits. The other ramifications of internal devaluation were sharply elevated levels of poverty, and in the cases of Latvia and Lithuania, previously discussed demographically unsustainable levels of emigration. In short, the working and middle classes paid nearly all the costs of adjustment to a crisis, which in large measure was itself a repercussion of the liberalization of the EU that privileged the interests of finance capital over
societal integration. In financialized economies social benefits are withdrawn, employment informalized, and the middle class is de-professionalized. For developed countries this marks the end of the theory of the marginal productivity of labor, which posits that wages ‘naturally’ rise in tandem with rising labor productivity. The ultimate irony is that this process reached its apotheosis in the Baltic states, which have been both ardent advocates of and a collective zone of experimentation for the most socially hostile forms of neoliberal policy.

Estonia was the first Baltic state to introduce the euro in 2011. Its early adoption conferred benefits in the form of confidence among new investors leading to FDI. Neighboring Finland, being in the euro, also provided further opportunities to integrate their respective economies. What benefits existed from euro membership were a function of timing as the first Baltic state to join, and its unique relationship to Finland. Neither of these factors was replicable by the other two Baltic states. Latvia’s January 2014 entry, despite majority opposition of its population, realized a long-term ambition of its political elite. Benefits of the euro from the perspective of neoliberals were enforced debt and inflation limits, along with further integration into Europe. As the Baltic’s second entrant, FDI benefits proved disappointing however (Baltic News Network, 2015a). Moreover, FDI projections for 2014 led to uncharacteristic calls from the Central Bank governor to stimulate the economy (Baltic News Network, 2015b). This *volte face* had more than a small odor of panic about it on the part of Latvia’s financial policymakers.

The two favored arguments proposed in defense of the euro on the cusp of implementation in 2014 were first, simply, ‘business wants it,’ as Latvia’s President Andris Berzins reported matter-of-factly (Pavliva, 2013), and second, as former two-times Prime Minister Aivars
Godmanis saw it, the Latvian economy was prone to ‘regular banking crises, happening every five to seven years,’ and that euro membership would permit them to exchange Latvian bank assets (often of dubious value) with those of the European Central Bank (ECB). Godmanis elaborated further stating that ‘up to 50% of deposits in Latvian banks belong to non-residents, and there are many reasons why they might want to withdraw their money’ *(Baltic Course, 2013)*. Government denials of being a ‘Cyprus 2.0’ offshore financial haven for funds of dubious origin rang somewhat hollow in the face of compelling evidence to the contrary *(21st Century Wire, 2014)*.

Meanwhile, Lithuania advanced its failed previous attempt to gain entry into the euro in 2006. The country almost fulfilled the admission criteria, but was rejected for failing to meet convergence criteria by a narrow margin, at a point when the euro project was at its peak confidence and could be selective on admission. Since the financial shock of 2008, with the euro’s luster much dulled, Lithuania’s January 2015 euro admission was presented to a hapless population as a reaffirmation of Lithuania’s irreversible orientation to the West. This given added urgency by the unfolding crisis in Ukraine in which Lithuania spearheaded nervous Baltic demands for an increased and permanent NATO presence. Over the course of 2014, FDI in Lithuania declined by more than two times compared to the previous year *(Baltic Course, 2015)*. With both Baltic neighbors to the north already in the eurozone and expected foreign investment inflows failing to materialize, Lithuania seems likely to receive a only a meagre ‘thirds’ at the FDI table.

By 2011, having emerged from the depths of crisis, the Baltic economies appeared to be on the road to rapid recovery with GDP growth reaching 8.3% in Estonia, 6.0% in Lithuania and 5.3% in Latvia, the fastest in the EU. This development was hailed, among others, by the Cato Institute as epitomizing ‘The Triumph of Good Economics’ *(Bandow, 2013)*. One
reason for this recovery was that wages in all three Baltic states, although growing in certain sectors largely as a result of emerging labor shortages, were still considerably below EU averages by as much as five or six times, and offered a significant competitive advantage. Other factors that facilitated apparent recovery were the continuing large transfers of EU Structural Funds and tax dumping via the torrents of offshore money coming from the CIS into Latvia and other parts of the Baltics. Increasing agricultural exports, especially of wheat and processed foods, along with timber also helped, as well as some revival of domestic demand, at least until EU sanctions on Russia over the conflict in Ukraine provoked a retaliatory trade embargo in which the Baltic states as agricultural exporters were particularly exposed.

By 2015 it had become apparent that the early rebound in GDP growth was unlikely to be sustained. In Latvia, GDP growth declined in 2014 to 2.4% from 4.2% in 2013. Independent forecasts for Latvia revised downwards previous estimates of 2.6% for 2015 to a more modest 1.9% growth (Swedbank, 2015a, p. 36; World Bank, 2015). Lithuania recorded average GDP growth of 3.3% per year from 2012 to 2014. However, a revised estimate for 2015 forecast a more modest 2.3% (Swedbank, 2015a, p. 40). As Swedbank analysts pointed out, potential economic growth in Lithuania was ‘now two times lower than it was before the crisis’ and ‘has been dragged down by a rapid shrinking of the labour force and employment, as well as by business underinvestment’ (Swedbank 2015b, p. 17). GDP forecasts for Estonia of 2.0% in 2015 were a modest 0.1% improvement on 2014 (Swedbank, 2015a, p. 34).

Looking forward, upbeat forecasts from the European Commission staff have predicted renewed upturn in 2016 (European Commission, 2015a, b, c). However, it appears to be that an enduring recovery is compromised, not simply by wider external uncertainties resulting from the general slowdown in the European and global economy, compounded by
geopolitical developments in the East, but also more importantly, by the profound internal demographic imbalances. Falling labour supply as a result of ‘exit’ has reduced a key incentive for productive foreign investment and impedes domestic recovery, with employers increasingly complaining of labour shortages. Thus, the future for the Baltic countries, especially in terms of moving up the added-value production chain, has been largely foreclosed by the impacts of austerity on labour. The migration consequences of internal devaluation are driving this trajectory of decline.

Social Europe renewed?

The failure of a European ‘social dimension’ at the moment of testing has required some further policy response, if only to re-establish the legitimacy of the European project in the eyes of its austerity-weary populations. It is at this juncture that ‘the specter’ of a Social Europe has appeared once more. The project of a Social Europe, the distinctive model elaborated first by Jacques Delors in the late 1980s, had its epitaph written by the crisis, not least by Mario Draghi, former Goldman Sachs advisor and President of the ECB (Wall Street Journal, 2012). The European Social Model is ‘gone’ proclaimed Draghi in summary form, much to the chagrin of key social partners such as European TUC (Ségol & Kirton-Darling, 2014). Such candor reveals much that has been previously unspoken, that the European social model was ‘depicted as unaffordable and burdensome’ in the face of the need for ‘fiscal consolidation’ (ILO, 2014).

In the backwash of the crisis, the European Commission has predictably returned to the ‘social dimension’ of the European project. Indeed, the ghost of a Social Europe is being resurrected at a time when its reality has almost entirely dematerialized. In the words of then Commissioner László Andor, DG Employment, Social Affairs and Inclusion, Social Europe
is necessary in order to ‘promote economic, social and territorial cohesion, and solidarity among the Member States’ and to enable a ‘long term reconstruction of the European Social Model’ in a Europe which is increasingly ‘polarized’ between the core and the periphery (Andor, 2013). As Andor put it:

This polarization is particularly marked within the euro area, where currency devaluation is no longer an option. As the sole remaining options for restoring their competitiveness, the euro-area Member States are left with internal devaluation or the loss of population through emigration.

Rather than reinforcing social protections and common standards, the European Commission talked of ‘developing guidelines on the design of labor market policies during the crisis’ (European Commission, 2009). Yet only in 2013, when talking up European economic recovery began to assume the character of a monotonous, even forlorn, incantation, did the Commission finally turn its long-overdue attention to Europe’s social dimension.

The ensuing Communication from the European Commission was titled, *Strengthening the Social Dimension of the Economic and Monetary Union* (European Commission, 2013). This proposed a renewed and enhanced role for social partners (employers and trade unions) in a revived social dialogue to address the downsides of austerity. To this end, the Commission proposed a scoreboard of social indicators. These indicators related to unemployment, specifically the numbers of young people not in employment, education, or training (the so-called NEETs). Other key indicators were the percentage of the working age population at risk of poverty and income inequality as measured by comparing the richest fifth of the population with the poorest fifth (the so-called income quintile ration), and the real gross
disposable income of households. Thresholds, both in terms of deviations from the euro area average as well as in terms of deviations from the historical values for any particular country, would be defined. If indicators exceed these thresholds, the Commission would undertake in-depth assessments for the countries concerned. These would provide the basis for future ‘coordinated’ employment and social policy interventions in the periodic round of advisory measures and recommendations from the Commission to member states (Country Specific Recommendations) in order to ‘better reflect the social implications of macroeconomic imbalances’ (Andor, 2013).

By contrast to the magnitude of the socio-economic challenges facing Europe, the renewal of the Social Model depends on policy implementation through an array of non-mandatory ‘soft’ steering tools, benchmarking processes, guidelines and recommendations within the so-called ‘European semester’ (Council of the European Union, 2013). These do not begin to match, never mind remediate, the costs of the rigid financial and fiscal interventions imposed on member states such as the Baltic countries that found themselves in the eye of the recessionary storm. Austerity has resulted in significant increases in poverty, with Latvia in 2013 having over one third of the population at risk of poverty (35.1%), while Lithuania has nearly one third (30.8%), and even slightly better-performing Estonia, nearly one quarter (23.5%) which approximates to the EU 28 average (24.5%) (Eurostat, 2014). At the same time, income inequality in the Baltic states (at least that income which is measurable) is among the highest in the EU, while average wages are the lowest in the EU (apart from Bulgaria and Romania), at 1038 euros per month in Estonia, 696 euros per month in Lithuania, and 604 euros per month in Latvia, (Trading Economics, 2015). In addition, a sizeable proportion of the workforce (between a fifth and a quarter) is officially paid at minimum monthly wages, which in 2015 amounted to 360 euros in the case of Latvia, 325
euros in Lithuania and 355 euros in Estonia (Eurostat, 2015). For these workers, ‘flexibility’
means unofficial informal ‘envelope’ wages, as well as being subject to employer abuse and
discriminatory preferences.

Nevertheless, the Communication was remarkable in being the first explicit recognition that
internal devaluation had entailed significant social costs. However, the message of
Commissioner Andor may have been somewhat overshadowed by that of former European
Commission President José Manuel Barroso who chose to launch yet another periodic high-
profile drives against unnecessary Brussels ‘red tape’ simultaneously to the release of the
Communication (BBC, 2013). Barroso’s successor as President of the European Commission,
Jean-Claude Juncker, assuming the mantle of architect of the post-crisis recovery in June
2014, has done even less to give tangible momentum to a renewal of Europe’s social
dimension. Juncker, a consummate Brussels ‘insider’ and a key architect of the Maastricht
treaty, was prominent as former Minister of Finance for Luxembourg, in attempting to
mobilize a concerted response during the Euro-crisis among his fractious and hesitant peers.
So glaring has been the policy vacuum that has ensued in terms of addressing the social
inequities of austerity, that a self-appointed ‘High-Level Group’, comprising among others
former Commissioner Andor, as well as his own predecessor at DG Employment and Social
Affairs, Anna Diamantopoulou, along with a host of European notables, felt constrained in
the Spring of 2015 to issue a report entitled ‘Unequal Europe’ calling for ‘a more caring EU’
(Friends of Europe, 2015). The intervention acknowledged that ‘Social Europe has been
slipping down the EU’s policy agenda last year’ and that this had ‘impelled Friends of
Europe to convene a high-level yet heterogeneous group of experts to analyse the facts and
propose solutions’ (Friends of Europe, 2015, p. 11). Among their recommendations,
addressing issues of labour mobility and migration, were measures to ‘define minimum
standards of European labour conditions and social protection, taking into account all new forms of labour like part-time workers’, the monitoring of ‘the implementation of the enforcement directive on the posting of workers’, and…the gradual introduction of ‘a guaranteed wage floor’ (Friends of Europe, 2015, p. 32). This latter, while figuring in Juncker’s election campaign for EU Presidency had since been quietly dropped. Timely as the report on renewing the ‘Social Union’ was, especially in calling on the Commission to take ‘a far broader approach to social investment’, its proposals in so far as they break with a deregulatory consensus, appeared likely to receive a lukewarm reception.

Where the Commission has intervened decisively, it has done so in order to promote market-led priorities and supply-side economics. An example from Baltic Lithuania illustrates how the Commission has encroached on policy areas previously the preserve of sovereign states, such as national collective bargaining systems and employment protection legislation in a manner that would have been unthinkable prior to the crisis. Detailed annual Country Specific Recommendations on economic and employment policies are proposed by the Commission in the form of ‘integrated guidelines’ which Member States are ‘invited to take into account.’ In line with previous recommendations, the Commission has proposed for Lithuania in 2014 that:

A comprehensive review of the labor law, with the involvement of social partners is needed to find ways of alleviating the administrative burden on employers. Primarily it will be essential to identify and eliminate unnecessary restrictions affecting flexible contractual agreements, dismissal provisions and working time arrangements (Council of the European Union, 2014).

Legal experts in Lithuania have been duly tasked to propose draft amendments which in the view of trade unions further weaken the remaining protections of the Labour Code. Their
proposals would remove the requirement to enter into a written contract of employment, remove limitations on working hours under certain circumstances, permit further easing of dismissal procedures by reducing the dismissal notification period from two to one month (or two weeks for those employed less than twelve months), reducing or all but eliminating severance payments in some cases, as well as facilitating fixed-term and temporary contracts of employment (Baltic News Network, 2015c). Echoing similar proposals for the southern eurozone periphery, it would seem that Country Specific Recommendations are intended to promote radical labor flexibilization and intensified employment precarity as the new order of the day (Clauwaert & Schoemann, 2012). In the aftermath of crisis, the Commission has exercised intensified oversight (‘surveillance’) of national budgets through a variety of instruments in order to ‘foster economic growth and prevent excessive macroeconomic imbalances’ and to secure ‘growth friendly fiscal consolidation’ with the aim of boosting growth and competitiveness (de la Porte & Heines, 2015). As exemplified in the Lithuanian case however, the Commission has also driven the wider deregulation of the labor market (Clauwaert & Schoemann, 2013; Degryse, Jepsen & Pochet, 2014, p. 27). In this web of intensified neoliberal controls, restoring social and labor rights, the core provisions of a Social Model, have been subordinated to a new fiscal disciplinarianism to be implemented in Europe’s eastern and southern peripheries.

Conclusion

The Baltic austerity model emerged from a constellation of global forces responding to the global crisis of capital accumulation located at the terminus of the Bretton Woods order. Resolution of that crisis has resulted in the erosion of national sovereignty since the 1970s, accelerating more with the Washington Consensus of the 1990s, and faster still after the great financial crisis of 2008. The Baltic experience of internal devaluation has revealed the restrictions of monetary union and loss of national economic autonomy within that larger
framework and reveals an austerity model on offer for export to other crisis countries the world over. That said, while the woes of the peripheral Baltic states have not been uppermost in the minds of the architects of ‘recovery’ from the crisis, much public debate has ensued concerning the efficacy of austerity in creating conditions for renewal of economic growth, not least in the southern eurozone countries. In part, this debate has also brought into renewed focus the more general crisis of European democracy. While austerity has become increasingly politically contested, the response of the Brussels elite appears to be repetition of the mantra of ‘more Europe, not less.’

In an ironic twist, ex-Prime Minister Dombrovskis of Latvia was rewarded for successfully steering of his country to full euro membership by being appointed as one of six Vice-Presidents of the new Commission. The ‘mission’ offered by Juncker to Dombrovskis placed the revival of a European social dimension at far remove from the renewal of the collective rights of labor and social protections that have been undermined by austerity. Dombrovskis was given responsibility for both the euro and for European social dialogue (European Commission Mission Letter, 2014). By default, the austerity ‘lessons’ of the Baltic model, were anchored in the highest reaches of the Commission.

Paradoxically, given the dominance of neoliberal currents from the very outset of post-communist reconstruction among the political and economic elites of the Baltic states, it is hard to say that their leaderships would have chosen another path, even if they were not constrained by EU fiscal and monetary directives and the pursuit of eurozone membership. How much responsibility should ultimately be apportioned to the European Commission or international bankers therefore, and to what extent it has been convenient for political and economic elites in these countries to claim that ‘their hands are tied’ is perhaps debateable.
Either way, the recipe of ‘internal devaluation’ applied with unflinching determination, whether externally imposed or willingly embraced, has produced apparent but probably only temporary macroeconomic stability. Yet, the costs in terms of damage to the social fabric of the Baltic states suggest that even this ‘victory’ for austerity may be a pyrrhic one.

Finally, with European policy circles seemingly wedded to the narrative of ‘successful’ internal devaluation (Baltic-style), it is important to reiterate that its trajectory has been predicated on a unique set of circumstances. These specific preconditions have been weak civil society and the demobilization of collective opposition, especially that of organized labor. Meanwhile, the export of an *austeriat* (in a perverse form of ‘free movement’) has reduced political pressures favoring alternative anti-austerity politics. If workers previously ‘voted with their feet’ in response to the ‘social failures of enlargement’ (Meardi 2012), an *austeriat* is now stampeding towards the exit door in response to the ‘social failures of austerity’. Continuing simplistic reiteration of the narrative of success of the Baltic model of austerity is contradicted by its societal costs, unequally borne by labor as against capital. An undeviating commitment to crisis resolution on current neoliberal disciplinarian terms by the current European Commission (and the international financial community) ensures that ultimate social (and economic) failure of austerity policies in the Baltic states will become a shared failure of the entire European Union project.

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